TARP's Hard Line on Executive Compensation: Misaligned Incentives and Constitutional Hurdles

JEREMIAH THOMAS*

TABLE OF CONTENTS

I. INTRODUCTION 1308
A. *The Origins of a Government Bail Out* 1310
B. *Responding to Banking's Arrogance* 1312
C. *Assessing TARP's Constitutional and Administrative Viability* 1314
II. CONSTITUTIONAL BACKGROUND 1316
A. *An Historical Examination of Governmental Impairment of Private Contracts* 1318
B. *Modern Standards for Applying the Contract Clause* 1320
C. *The Fifth Amendment and Contractual Commitments* 1321
1. *The Taking of a Contractual Right* 1322
2. *Property Deprivation and Due Process* 1323
D. *The* Gold Clause Cases 1324
III. THE CONSTITUTIONAL LIMITATIONS FOR EXECUTIVE COMPENSATION REGULATION 1327
A. *The Constitutionality of Golden Parachute Restrictions* 1327
1. *Revisiting* Blaisdell*: "Moratoria" on Golden Parachute Payments* 1330
2. *At What Point Would TARP's Restrictions Amount to a Taking?* 1332
3. *Will Golden Parachutes Be Grounded for Good?* 1333
B. *The Constitutional Implications of Salary & Bonus Limits* ... 1335
1. *Constitutional Hurdles for Prospective Guidelines* 1336
2. *The Ominous Effects of Retrospective Regulation* 1338
IV. THE ADMINISTRATIVE AND ECONOMIC PITFALLS OF COMPENSATION LIMITS 1341
A. *Administering a Complex Regulatory Scheme* 1341
B. *Economic Incentives—and Disincentives—Provided by Executive Compensation Limitations* 1346

---

* J.D. Candidate, 2010, The Ohio State University Moritz College of Law. I want to thank Professor Paul Rose for his comments, which were very helpful in preparing this Note. I would also like to thank Matthew Chisman, Matthew Elliott, and Michael Von Ansbach-Young for providing me with a sounding board for my ideas.

V. CONCLUSION: MOVING FORWARD WITH LITTLE GUIDANCE AND BIG GOALS 1351
A. *How Can the Treasury Department Responsibly Implement Current Policies?* 1351
B. *What Should Congress Do to Alleviate Self-Created Problems?* 1353
C. *In What Ways Can Individuals and Companies Protect Their Interests?* 1355
1. *Protecting Institutional Interests* 1355
2. *Protecting Individual Interests* 1356
D. *Moving Forward* 1358

I. INTRODUCTION

It is a familiar feeling. Late hour, dark night, and you are at the ATM cautiously looking over your shoulder for fear of being robbed . . . by your bank's CEO. That very fear, or the political penumbra of it, prompted Congress to address this infamous rash of thieving CEOs with restrictive provisions on executive compensation while constructing the Troubled Assets Relief Fund (TARP)[1] and subsequent legislation. The enactment of these restrictions gives rise to several legal and practical questions: Are the restrictions effective? Do they punish (or regulate) the right people? What will these restrictions really do? And perhaps most importantly, are they even enforceable?[2]

Members of Congress have taken their turn attacking CEOs of the banks in a public display of outrage more suited for the perpetrators of a Ponzi scheme than for the respected executives of the financial community.[3] Representatives, Senators, and even the President have expressed displeasure with the apparent excesses enjoyed by the executives of this nation's failing

---

[1] *See* Emergency Economic Stabilization Act of 2008, Pub. L. 110-343, 122 Stat. 3765, 3776–77 (to be codified at 12 U.S.C. § 5221) [hereinafter EESA]; American Recovery and Reinvestment Act of 2009, Pub. L. 111-5, § 7001 (amending EESA § 111 *et. seq.*) [hereinafter ARRA].

[2] TARP's current statutory scheme regarding executive compensation is the result of two overlapping, and in some ways conflicting, statutes passed within five months of each other. It is beyond the scope of this Note to consider how TARP would be administered if a court were to find some or all of its provisions unenforceable.

[3] *See* Steve Holland & Karey Wutkowski, *Wall St. CEOs Berated by Lawmakers*, REUTERS, Feb. 12, 2009, http://uk.reuters.com/article/governmentFilingsNews/idUKN1137220820090212.

financial institutions.[4] Venom, disbelief, and scorn have been spat upon the industry for its continued utilization of a compensation structure, heavily weighted with bonuses and light on salary, where much of an individual's income is paid on a discretionary basis.[5] With hundreds of billions in taxpayers' dollars invested into the banking industry,[6] and trillions more pledged in various loan guarantees,[7] it is not surprising that lawmakers might question how that money was being used by the companies. It is equally unsurprising that Congress responded to these concerns by targeting the symbol of the banking industry's arrogance, executive compensation.[8]

As is often the case when government takes drastic action to address a broad social problem, many questions about the efficacy of TARP's design and implementation remain open. Much time has been devoted to discussing whether the bail out package was the appropriate size.[9] Pundits have wrangled over whether government functioned in its appropriate role when it began pumping money into private banks in the first place.[10] But few of

---

[4] *See* Sheryl Gay Stolberg & Stephen Labaton, *Bankers' Bonuses Are 'Shameful', Obama Declares*, N.Y. TIMES, Jan. 30, 2009, at A1.

[5] *See, e.g.*, Colin Barr, *Who Cares If Wall Street 'Talent' Leaves?*, CNN, Oct. 23, 2009, http://money.cnn.com/2009/10/23/news/newsmakers/fed.feinberg.fortune/index.htm?postversion=2009102310.

[6] *See* EESA § 115 (a).

[7] *See* Mark Pittman & Bob Ivry, *U.S. Pledges Top $7.7 Trillion to Ease Frozen Credit*, BLOOMBERG.COM, Nov. 24, 2008, http://www.bloomberg.com/apps/news?pid=20601109&sid=an3k2rZMNgDw&refer=home.

[8] *See* John Hendren, *Obama: Wall Street 'Arrogance and Greed' Won't Be Tolerated*, ABC NEWS, Jan. 31 2009, http://abcnews.go.com/Politics/CEOProfiles/Story?id=6778419&page=1. As this Note goes to print, both Houses of Congress are considering legislation that would mandate stronger corporate governance controls over executive compensation giving shareholders more "say on pay." *See* Kevin Drawbaugh, *WRAPUP 1—U.S. Sen Dodd Offers Bold Financial Reform Plan*, FORBES.COM, Nov. 10, 2009, http://www.forbes.com/feeds/afx/2009/11/10/afx7107719.html.

[9] *Compare* Holman W. Jenkins, Jr., *Obama's Dangerous Bank Bailout*, WALL ST. J., Feb. 4, 2009, at A11 (arguing that a minimal investment in most banks would have protected borrowers, creditors, and account holders and subjected shareholders only to a delayed realization of their investment), *with* Edmund L. Andrews & Eric Dash, *Deeper Hole For Bankers*, N.Y. TIMES, Jan. 14, 2009, at A1 (reporting on Fed. Chairman Ben Bernanke's belief that the initial $700 billion dollar bail out would be insufficient to fully stabilize the nation's economy).

[10] *See, e.g.*, Jeffrey A. Miron, *Commentary: Bankruptcy, Not Bailout, Is the Right Answer*, CNN, Sept. 29, 2008, http://www.cnn.com/2008/POLITICS/09/29/miron.bailout/. Even some pre-TARP actions were informed by this discussion over the government's role. The Treasury's failure to prevent the bankruptcy of Lehman Brothers, for instance, was reportedly due in part to concerns that such action would exceed federal

TARP's potential issues have garnered less critical inspection than its executive compensation limitations.

Questions remain concerning the constitutional viability of the plan's restrictions on executive compensation. Many hurdles also stand in the way of the fair administration of TARP, both procedurally and substantively. Additionally, the unintended social and economic implications of the regulatory scheme for executive compensation are to this point unexplored. This Note attempts to address those three issues and provide strategic guidance through which the various institutional players can minimize the negative effects of TARP's shortcomings.

A. *The Origins of a Government Bail Out*

In the wake of the near collapse of the US banking industry, legislators enacted a two stage cash infusion directed toward struggling banks that totaled $700 billion.[11] Though initial proposals for this infusion envisioned the federal government purchasing "toxic" mortgage-backed securities to remove the troubled assets from the balance sheets of struggling institutions,[12] the Treasury and Congress eventually decided to utilize preferred share purchases in selected financial institutions as the primary method for disbursing the first half of the TARP funding.[13] This shift in focus was driven by several factors, not the least of which was recognition that pricing "toxic" securities would be a difficult task given that the housing market was then in a downward spiral and that many of the securities in question were derivative financial instruments that included fractional pieces of many mortgages.[14]

Once the decision was made to utilize equity and not asset purchases, the Treasury began inserting covenants into the stock purchase agreements; these

---

authority to protect the banking system (Lehman Brothers was primarily a brokerage house and not a bank). *See* Joe Nocera & Edmund L. Andrews, *The Reckoning: Running a Step Behind as a Crisis Raged*, N.Y. TIMES, Oct. 23, 2008, at A1.

[11] EESA § 115(a).

[12] *See* Press Release, U.S. Treas. Dept. Office of Public Affairs, Fact Sheet: GSE Mortgage Backed Securities Purchase Program (Sept. 7, 2008), *available at* http://www.treasury.gov/press/releases/reports/mbs_factsheet_090708hp1128p.

[13] *See* Sudeep Reddy, *Real Time Economics: The Evolution of Henry Paulson*, WALL ST. J. ONLINE, Oct. 14, 2008, http://blogs.wsj.com/economics/2008/10/14/the-evolution-of-henry-paulson/.

[14] *See* John Waggoner & Matt Krantz, *Pricing Mortgage-Backed Securities Will Be Tough*, USA TODAY, Oct. 7, 2008, http://www.usatoday.com/money/industries/banking/2008-09-23-toxic-paper-bailout_N.htm.

covenants restricted fund recipients from paying certain bonuses and all golden parachute payments to top executives—at least while the Treasury maintained equity interest in a company[15] Congress provided a legal backstop for these agreements by codifying specific restrictions concerning executive compensation, including restrictions on golden parachute payments.[16]

Little negative attention was paid to these initial restrictions, in part due to several years of unenthusiastic press surrounding the exorbitance of golden parachute packages.[17] Legal and business scholars had already engaged in years of debate over whether and how golden parachute rights could be limited,[18] and the financial emergency faced by troubled banks provided an easy test case for reeling in these provisions. The fact that Congress, at least initially, limited only the *payment* of golden parachute consideration, and only during the time the bank was using capital invested by taxpayers, lent an air of reasonableness that shielded the legislation from political punditry on both sides of the isle. Once it had a foothold, of course—and by mid-2009—Congress was looking to expand compensation oversight to affect a broader array of publicly traded companies.[19]

---

[15] *See, e.g.*, Securities Purchase Agreement § 1.2(d)(v), Bank of America, Oct. 26, 2008, *available at* http://www.financialstability.gov/docs/agreements/BOA_10262008.pdf. Despite this broad authority, many critics have argued that the actual implementation of these restrictive policies has fallen far short of initial expectations. Declan McCullagh, *Other People's Money: Cracks in TARP Bailout Show Its Problems*, CBS NEWS, Dec. 4, 2008, http://www.cbsnews.com/stories/2008/12/04/politics/otherpeoplesmoney/main4647109.shtml. Especially during the early months of the bailout, many believed that the Treasury Department had done little to ensure that banks receiving TARP funds were in fact complying with the bonus and golden parachute provisions of the Bill. *See id.*

[16] *See* EESA § 111.

[17] The public now typically views these payments as the cost of getting rid of a well-compensated, but underperforming, CEO or other executive officer. This perception grew from a string of very large pay-outs aimed to oust executives after periods of declining revenues and plummeting share prices. *See* Lucian A. Bebchuk & Jesse M. Fried, *Pay Without Performance: Overview of the Issues*, 30 J. CORP. L. 647, 649 (2005). Whether TARP's harsh treatment of golden parachute clauses is overbroad will be addressed *infra* Parts III & IV. Nevertheless, it is worth noting that under the EESA and subsequent regulation, the definition of "golden parachute" has expanded broadly to include many types of severance payments to executives. The scope of this expansion will be explored later in this Note.

[18] *See* Bebchuk & Fried, *supra* note 17, at 649.

[19] *See* Tomoeh Murakami Tse, *Wall St. Jacks up Pay After Bailouts: Lawmakers Warn Against Return to Pre-Crisis Levels*, WASH. POST, July 23, 2009, *available at* http://www.washingtonpost.com/wp-dyn/content/article/2009/07/22/AR2009072203687.html.

B. *Responding to Banking's Arrogance*

Though few dispute that there is something unsavory about millionaire executives cashing in large severance or bonus packages in the wake of near financial collapse, the fact remains that the terms of those bonuses were often guaranteed far in advance of any financial turmoil.[20] Executives that had provided years of leadership through booming economic times now felt entitled to the fruits of the contracts that they had originally negotiated as a protective measure to secure the value of their successes in the event of unforeseen failure.[21] In the immediate period after the release of the first round of TARP funding, at least some such executives chose to eject from their metaphorical cockpits and open their golden parachutes before their struggling employers received federal funds.[22] This activity attracted little public attention, especially when compared to the nearly twenty billion aggregate dollars reportedly paid out in bonuses by banks to employees at the end of 2008.[23]

As the government set to release the second half of TARP funding at the beginning of 2009, the 2008 bonuses sparked a new rallying cry in favor of strict federal oversight in the banking industry.[24] Newly inaugurated President Obama referred to the bonus expenditure by the troubled banks as "shameful" behavior.[25] President Obama and Treasury Secretary Timothy Geithner unveiled a plan to combat these shameful tactics with a $500,000 annual cap on executive compensation for firms that had received

---

[20] *See* Bebchuk & Fried, *supra* note 17.

[21] *See* Paul Kiel, *Bank Got Bailout, CEO Got Golden Parachute*, PROPUBLICA, Nov. 19, 2008, *available at* http://www.propublica.org/article/bank-got-bailout-ceo-got-golden-parachute-1119.

[22] *Id.* For instance, Mack Whittle of South Financial Group, a regional bank based in South Carolina, stepped away from the company that he founded—roughly two months before he had planned—in order to collect on his 18 million dollar severance. *Id.* Shortly after his departure, South Financial Group accepted $347 million in government funds. *Id.*

[23] *See* Stolberg & Labaton, *supra* note 4 at A1.

[24] *Angry Senator Wants Pay Cap on Wall Street 'Idiots,'* CNN, Jan. 30, 2009, *available at* http://www.cnn.com/2009/POLITICS/01/30/executive.pay/index.html?iref=newssearch. Senator McCaskill, for instance, introduced legislation to statutorily limit the total compensation of all employees at institutions that had received any federal money to not exceed the salary of the President.

[25] *See* Stolberg & Labaton, *supra* note 4. President Obama went on to say that "[t]here will be time for them to make profits, and there will be time for them to get bonuses. Now's not that time. And that's a message that I intend to send directly to them, I expect Secretary Geithner to send to them." *Id.*

"exceptional" investment funds.[26] Companies that received investments from the "general" investment program could waive this annual cap, but only by seeking shareholder approval of the waiver.[27] The Treasury also moved to broaden the restriction on golden parachute payments to include "all severance" packages that exceeded one year of the executive's annual compensation.[28] Additionally, certain limitations were extended to apply to the top ten executives of the company (up from five under the EESA) and another twenty-five executives under certain specified conditions.[29]

Days after the President and Secretary of Treasury moved to address the supposed excesses of the banking industry, Congress lashed out to reign in executive compensation even further.[30] In the final compromise to a package referred to in the popular press as a "stimulus bill," Senator Dodd was able to successfully include provisions that further limited executive compensation.[31] In the bill, Congress went against presidential urgings and applied all new limitations retroactively to the 359 banks[32] that had received any federal funds at the time of the bill.[33] Additionally, the congressional plan further limited the methods by which executives could be paid, establishing an absolute cap on annual bonuses at one-third of the executive's annual salary.[34] Bonuses could no longer be paid in cash, and instead must be paid in company stock, redeemable only after the government no longer

---

[26] Press Release, U.S. Dep't of the Treasury, TG-15: Treasury Announces New Restrictions on Executive Compensation (Feb. 4, 2009) [hereinafter TG-15] (on file with author), *available at* http://www.ustreas.gov/press/releases/tg15.htm. Incidentally, the released restrictions failed to define what would qualify as "exceptional" aid. Most in the public generally accepted that only Citigroup, Bank of America, and AIG would be affected. *See* Roger Runningen & Hans Nichols, *Obama Orders Pay Limits at Banks Getting Future Aid*, BLOOMBERG.COM, Feb. 4, 2009, http://www.bloomberg.com/apps/news?pid=20601087&refer=home&sid=a6fHgp5yAPLw.

[27] *See* TG-15, *supra* note 26. This and most of the other Treasury restrictions would apply only to financial institutions that received additional money following the implementation of the regulations. *Id.*

[28] *Id.*

[29] *Id.* Under these restrictions, institutions that received "exceptional" financial assistance would be prohibited from paying any severance to the top ten executives of the company while the government maintained a stake. *Id.* The *next* twenty-five executives could receive severance, but no such payment could exceed one year's salary. *Id.*

[30] *See* Tomoeh Murakami Tse, *Congress Trumps Obama by Cuffing Bonuses for CEOs*, WASH. POST, Feb. 14, 2009, at A1.

[31] *Id.*

[32] *Id.*

[33] *See* ARRA § 7001 (amending EESA § 111).

[34] *Id.* (amending EESA § 111(b)(3)(D)(i)).

holds an equity stake in the employing company.[35] Additionally, the statutory limitations swept beyond the executive suite to affect many non-executive employees at the banks.[36] The definition of golden parachute payment was expanded to include "any payment to a senior executive officer for departure from a company for any reason."[37] Even the scope of the Treasury's oversight role was expanded, as the Secretary was required to review "bonuses, retention awards, and other compensation paid to the senior executive officers and the next 20 most highly-compensated employees of each entity receiving TARP assistance before the date of enactment" in order to ensure that those payments comported with the retroactive mandate of the restrictions.[38] The Treasury Department was even empowered to negotiate the clawback of bonus payments, and money collected was to be paid to the government, not to the employer bank![39] More regulation and repeal would follow, but the stage was set for a battle between TARP's administrators and the individuals in charge of TARP's participating institutions.

C. *Assessing TARP's Constitutional and Administrative Viability*

As the regulatory framework surrounding executive compensation at troubled financial institutions grew, so too did the obstacles to the fair and orderly implementation of the provisions. After the initial restrictions upon golden parachute provisions were signed into law, there were some rumblings about impermissible interference in private affairs.[40] But as more

---

[35] *Id.*

[36] *Id.* In fact, even based upon February 2009 investment levels, the graduated application of the bill would result in *annual compensation* restrictions for nearly four thousand bank employees. *See* OFFICE OF FINANCIAL STABILITY, U.S. TREASURY DEP'T, TRANSACTIONS REPORT (Feb. 10, 2009), *available at* http://www.financialstability.gov/docs/transaction-reports/transaction_report_02-10-09.pdf [hereinafter Transactions Report]. That number pales in comparison to the number now affected, as by July 2009 the number of banks enrolled in the program had increased from 359 to 651. *See* Press Release, U.S. Dep't of the Treasury, TG-215, Treasury Releases May Monthly Bank Lending Survey (July 15, 2009), *available at* http://www.ustreas.gov/press/releases/tg215.htm. In contrast, the initial TARP restrictions would have affected only the *exit packages* of roughly 1500 senior executives.

[37] ARRA § 7001 (amending EESA § 111(a)(2)).

[38] *Id.* (amending EESA § 111(f)).

[39] *Id.*

[40] *See* White & Case LLP, *Client Alert: The New Recovery Legislation: The TARP Covers Executive Compensation*, Oct. 2008, *available at* http://www.whitecase.com/files/Publication/ae422fc2-5b3b-404f-b294-f3756dce846d/Presentation/PublicationAttachment/c10e65c2-9d26-4744-ae76-0378aa41420e/Alert_ECBEL_FMD_100308_4.pdf.

restrictions followed, so did increased constitutional concerns.[41] What began as a simple policy to prevent individual executives from profiting in the face of poor decision making grew into a full-fledged regulatory scheme aimed more toward promoting the quick repayment of federal money.[42] And though the strategy seemed simple enough—withhold money from key employees at each financial institution in order to motivate the speedy repurchase of government interests—the implementation of the executive compensation limitations created a complex web of constitutional questions, strategic planning hurdles, and economic disincentives for investing in troubled firms.[43]

The implementation of such a restrictive regulatory regime raises several questions. To what extent can the government regulate corporate behavior by abrogating individual contractual rights? How can the Treasury Department properly administer TARP considering its complex restrictions? What are the intended and unintended economic consequences that result from the executive compensation provisions?

The next section of this Note, Part II, specifically addresses the federal government's power to interfere with individuals' contractual rights. The question harkens back to the years following the Great Depression when Congress exercised unprecedented influence over the economic affairs of the nation.[44] Included is a discussion of the historical lineage of contractual

---

[41] *See* Fried, Frank, Harris, Shriver & Jacobson LLP, *Congress Sets New Executive Compensation Limits for TARP Recipients*, 21ST CENTURY MONEY, BANKING & COMMERCE ALERT, Feb. 19, 2009, *available at* http://www.ffhsj.com/siteFiles/Publications/37F8269D146E9D4AF75E624D0DD6FFCC.pdf.

[42] *See* Tse, *supra* note 30.

[43] *See* White & Case LLP, *supra* note 40.

[44] Although much has been made of the economic connection between the bank collapse of 2008 and the Great Depression following a market crash coupled with a failure of the banking system, it is important to remember the many differences between the two circumstances. *See* Ira Artman, *Great Depression vs. 'Great Deleveraging'—Can You Tell the Difference?*, SEEKING ALPHA, Feb. 26, 2009, http://seekingalpha.com/article/122842-great-depression-vs-great-deleveraging-can-you-tell-the-difference?source=reuters. First, the banking crisis of the Great Depression was fueled by a "run" on bank deposits, a phenomenon that has no parallel in the present crisis because of the advent of FDIC-insured institutions. *Id.* Second, the federal government passively watched while banks failed during the Great Depression, exacerbating the effects of the massive account withdrawals. *Id.* The government's current strategy to infuse cash into struggling banks counteracts the potential for such a spiral. *Id.* Finally, taxes were increased by more than double for top wage earners during the Depression, further reducing the amount of capital available for private investment. *Id.* Tax rates during the current crisis have flattened, and in some instances decreased. *Id.* Moving forward, the largest suggested tax increase for families with an income exceeding one million dollars has been 5.4%. *See House Plan*

protections under the Constitution. Following the history, there is a description of several related doctrinal frameworks applied by courts to assess the validity of contract regulation.

Part III of this Note endeavors to apply the doctrinal frameworks developed in Part II to various provisions of TARP that effect private contracts and other property rights. The section considers three applications of constitutional principles regarding TARP's restrictions on golden parachute payments. The section also contemplates the constitutional vulnerability of TARP's salary and bonus restrictions, expressing particular concern over the retroactive application of guidelines contained in the February 2009 stimulus bill.

Part IV of this Note provides a broad, but comparatively brief, analysis of the economic and administrative viability of the regulatory scheme. It begins with an examination of the complexities that will be navigated by the overseeing Treasury Department. The section continues by exploring what individuals and institutions could become parties in an action concerning compensation restrictions. What follows is a look at the potentially devastating economic impact certain compensation restrictions could have on the funded institutions. The section closes with an inspection of whether the economic incentives created by the compensation restrictions act to further or inhibit the purposes of TARP.

The Note concludes by suggesting a course of action for the various players involved in the administration of the executive compensation provisions. It suggests some legal and strategic devices that the Treasury Secretary may employ, on the one hand to avoid litigation, but more importantly to maintain constitutional legitimacy during the government's hopefully limited foray into bank ownership. Congress is also urged to address certain aspects of the existing law, both to ensure favorable constitutional outcomes and to provide a logically consistent set of incentives that coincide with TARP's purposes. Finally, some direction is provided to executives, other highly compensated employees, and their employer-institutions as to how to tackle the restrictions currently placed upon their relationships. Some consideration is given as to which parties are best suited to mount challenges to the current provisions and also to the best methods through which a challenge could be mounted.

II. CONSTITUTIONAL BACKGROUND

A surface examination of the economic and political realities that precipitated TARP re-affirms congressional intuition that taxpayer money

---

Boosts Taxes on Rich to 20-Year High, MSNBC, July 15, 2009, http://www.msnbc.msn.com/id/31927196/ ns/politics-capitol_hill/.

should not be funneled, directly or indirectly, into the pockets of executives who were at least complicit and at most responsible for the onset of financial crisis. But congressional power is not a function of political expediency.

Since the signing of the Constitution, the legislative bodies of this country have been generally forbidden from interfering with the obligations contained in legally executed contracts by the Contract and Due Process Clauses.[45] Until World War I, few courts had found sufficient justification to depart from this general rule.[46] Following the Great Depression, however, several doctrinal frameworks emerged through which governmental interference with private contracts would be evaluated. Because the history and policy justifications for protecting contractual rights inform any discussion of its current application, this section starts with a description of the lineage of the constitutional protection of private contracts. Following the historical overview, the discussion will shift to an examination of viable doctrinal frameworks, beginning with Contract Clause jurisprudence,[47] continuing through two distinct applications of the Fifth Amendment,[48] and concluding with a discussion of seldom invoked precedent involving the "emergency" power of Congress.[49]

---

[45] U.S. CONST. art. I, § 10, cl. 1; *id.* amend. V.

[46] *See* Omnia Commercial Co., Inc. v. United States, 261 U.S. 502 (1923) (holding that there is no remedy for a company that contracted with a manufacturer of steel when government requisitions all of the manufacturer's product during war time, making the contract impossible to execute).

[47] Though not directly applicable to federal action, the discussion may be very important to predicting a modern response to TARP's restrictions on compensation—as the federal government has seldom forged so deeply into the waters of contract impairment. *See* discussion *infra* Part II.A (commenting on the historically limited powers of the federal government). Contract Clause jurisprudence is much better developed than federal jurisprudence in the same area, and—should a court be faced with such a case—courts may look to borrow principles from this area for modern application.

[48] The first leg of the Fifth Amendment discussion considers the "taking" of a property right. *See Omnia*, 261 U.S. at 508 (acknowledging contractual rights as property under the meaning of the Fifth Amendment's Takings Clause). The second leg examines the property protections contained in the Due Process Clause. So little precedent and commentary exists concerning the substantive portion of this analysis that it is one of the most interesting questions facing the executive compensation provisions of TARP. Intuitively, congressional declaration that any individual could not collect on contractually guaranteed debt runs counter to the fundamental principles of individual liberty. The jurisprudence in this particular area is sparse and no consensus exists even with respect to what "property" is protected by the Due Process Clause. *See* Thomas W. Merrill, *The Landscape of Constitutional Property*, 86 VA. L. REV. 885, 890–92 (2000).

[49] This line of jurisprudence arose in 1935 after President Roosevelt and Congress put a freeze upon the gold trade. This freeze had the effect of frustrating many outstanding contracts that had contemplated payment be made in gold, and the resulting

A. *An Historical Examination of Governmental Impairment of Private Contracts*

The early years of our nation provided many reasons for both state and federal governments to discount private contractual rights in the face of economic emergency. The Revolutionary War had weighed heavily upon the American public due to both war time spending and various trade barriers imposed by the British during the course of the war.[50] States reacted by providing for sweeping debt relief for private individuals, and the resulting economic chaos exposed the relief programs as one of the largest failures of the Articles of Confederation.[51] Chief Justice John Marshall described the effects of the programs as follows:

> The power of changing the relative situation of debtor and creditor, of interfering with contracts . . . had been used to such an excess by the State legislatures, as to break in upon the ordinary intercourse of society, and destroy all confidence between man and man. The mischief had become so great, so alarming, as not only to impair commercial intercourse, and threaten the existence of credit, but to sap the morals of the people, and destroy the sanctity of private faith.[52]

It is against this dire backdrop that the Constitution was crafted.[53] Having learned from earlier disaster, the Framers included the Contract Clause and other property protections in the document.[54]

The principles behind those protections still inform legal scholarship today. First, fundamental to the Framers of the Constitution was the principle of private autonomy.[55] Abrogation of private contracts by legislative fiat

---

litigation has come to be known as the *Gold Clause Cases*. *See* ROBERT A. LEVY & WILLIAM MELLOR, THE DIRTY DOZEN: HOW TWELVE SUPREME COURT CASES RADICALLY EXPANDED GOVERNMENT AND ERODED FREEDOM 51 (2008) (citing Perry v. United States, 294 U.S. 330 (1935); Nortz v. United States, 294 U.S. 317 (1935); Norman v. Balt. & Ohio R.R. Co., 294 U.S. 240 (1935)). The cases provide a unique jurisprudential perspective that consider individual rights in light of government power, instead of the more conventional approach that considers the latter in light of the former. The analysis may prove particularly relevant in that the congressional power that the *Gold Clause Cases* address is the power to regulate the value of the nation's currency. *See* discussion *infra* Part II.D.

50 *See* LEVY & MELLOR, *supra* note 49, at 54–55.

51 *See* Ogden v. Saunders, 25 U.S. 213, 354–55 (1827).

52 *Id.*

53 *Id.*

54 *Id.*

55 LEVY & MELLOR, *supra* note 49, at 53.

inhibits individual liberty to dispose of labor and property as desired and private autonomy suffers as a result.[56] Second, fundamental principles of fairness demand that governmental rules apply only prospectively so that individuals can rationally plan their affairs without government intrusion.[57] When contractual rights are not honored, individuals are at risk to lose the consideration paid on one end of an agreement without collecting the agreed upon value from the other party. Finally, limiting the legislative power to the prospective regulation of contracts protects the judiciary's role as the sole arbiter of individual disputes.[58]

The impropriety of *state* intervention was so obvious to early Americans that the Constitution displays a textual commitment to proscribing such behavior from state governments.[59] Though a similar prohibition was not explicitly included with respect to the federal government,[60] the crafters of the Constitution recognized the universal importance of the sanctity of contracts.[61] The legally accepted principles at the time conceived a limited federal government; one that would only have the authority to impair contracts if the Constitution enumerated the power to do so.[62] In light of history, the absence of a federal contract clause may reflect a belief that no

---

[56] *Id.*

[57] *Id.* Although only applicable to criminal proceedings, this principle is reinforced by prohibitions on ex post facto laws. *See* U.S. CONST. art. I, § 9, cl. 3; *id.* art. I, § 10, cl. 1.

[58] *See* LEVY & MELLOR, *supra* note 49, at 53. In contrast to the judiciary, the legislature is entrusted with establishing a broader set of mechanisms through which multiple parties, indeed all of a given society, are to interact. *Id.*

[59] "No State shall . . . pass any Bill of Attainder, ex post facto Law, or Law impairing the Obligation of Contracts, or grant any Title of Nobility." U.S. CONST. art. I, § 10, cl. 1. This prohibition applies only to contracts already in existence at the time of the government action. *See* Ogden v. Saunders, 25 U.S. 213 (1827). For a brief time, the Court read the Contract Clause in concert with the Fourteenth Amendment to imply a fundamental right for private parties to enter into new contracts. *See* Lochner v. New York, 198 U.S. 45, 53 (1905). This interpretation has long been abandoned. *See, e.g.*, W. Coast Hotel Co. v. Parrish, 300 U.S. 379, 392 (1937) (the "freedom of contract is a qualified, and not an absolute").

[60] Congress is prohibited from passing Bills of Attainder, ex post facto Laws, and from granting Titles of Nobility, but a textual prohibition of federal laws impairing the Obligation of Contracts is conspicuously absent from the Constitution. *See* U.S. CONST. art. I, § 9.

[61] *See, e.g.*, THE FEDERALIST NO. 44 (James Madison) ("laws impairing the obligation of contracts are contrary to the first principles of the social compact, and to every principle of sound legislation").

[62] *See* THE FEDERALIST NO. 45 (James Madison). One such enumeration does exist, as Congress can provide for "uniform Laws on the subject of Bankruptcies." U.S. CONST. art. I, § 8, cl. 4.

need existed to prohibit the federal government from exercising a power that it did not possess. The Constitution's Framers envisioned a small role for the federal government, and it was some time before national policy began playing any significant role in the governance of such things as contracts.[63] Even if Congress properly invokes a constitutional justification for regulating existing contracts,[64] the Due Process Clause of the Fifth Amendment limits congressional authority to act without adequate justification.[65]

The Great Depression prompted a shift away from the absolute protection of existing contracts. In the face of massive foreclosures due to financial crisis and high unemployment, the Minnesota legislature enacted a statute that placed a two year moratoria on foreclosures of homes secured by mortgage for individuals that met certain conditions.[66] The Supreme Court case that ultimately upheld the State's action ushered in the modern era of contract impairment jurisprudence.[67]

B. *Modern Standards for Applying the Contract Clause*[68]

Under the terms of the Minnesota foreclosure statute, lending companies were entitled to "reasonable rental value" during the moratoria, but they were not entitled to exercise any property rights that existed as an incident of the mortgage contract and foreclosure statutes.[69] In upholding the Minnesota

---

[63] *See* McCulloch v. Maryland, 17 U.S. 316, 400–25 (1819) (recognizing that the powers bestowed by the Constitution upon Congress include "implied" powers which are necessary to effectuate the enumerated powers). That the federal government must constrain itself to specifically enumerated powers was so obvious that the principle went basically unchallenged for nearly thirty years, ending with this dispute between the state of Maryland and the Second Bank of the United States. *See id.*

[64] This Note presumes that passage of the Emergency Economic Stabilization Act of 2008, including its provisions concerning executive compensation, was pursuant to some constitutional authority. Such authority would almost certainly be recognized given the broad powers implied by the Commerce Clause. *See* U.S. CONST. art. I, § 8, cl. 3. In the unique circumstances surrounding the Act, additional authority may arguably exist due to Congress's power to regulate the value of currency. *See* U.S. CONST. art. I, § 8, cl. 5. The second potential justification may be particularly salient when contract impairment is at issue. *See infra* Part II.C (discussing the *Gold Clause Cases*).

[65] *See* Richard E. Speidel, *Contract Excuse and Retrospective Legislation: The Winstar Case*, 2001 WIS. L. REV. 795, 799.

[66] *See* LEVY & MELLOR, *supra* note 49, at 57–58.

[67] *Id.*

[68] Again, the lack of coherent jurisprudence regarding the federal impairment of contracts makes a discussion of Contract Clause principles highly relevant to predicting future development in this area. *See* Merrill, *supra* note 48 and accompanying discussion.

[69] Home Bldg. & Loan Ass'n v. Blaisdell, 290 U.S. 398, 416–17 (1934).

statute, the Supreme Court reasoned that the states retained the power to prescribe remedies for contractual breaches.[70] In defining the remedy for mortgages, Minnesota simply delayed the option of foreclosure without destroying the body of the contract.[71] Having interpreted the State's action as a delay for contract remedies, and not a destruction of contract rights, the Court found that the Minnesota legislation was reasonably related to the legitimate emergency the program was designed to address.[72]

Modern courts apply a three-part test to approximate the *Blaisdell* doctrine.[73] The court first examines whether state action has had the effect of substantially impairing a contract.[74] This inquiry is somewhat opaque but might be analogized to the determination of materiality with respect to contract law. If the court believes that the contract has been substantially impaired by state action, the state can counter by showing a "significant and legitimate public purpose" for its action.[75] Unlike in *Blaisdell*, this legitimate purpose need not be an emergency but must at least address "a broad and general social or economic problem."[76] Finally—even if the impairment does serve a legitimate goal—it still must be reasonable in light of the broad problem the state action intends to address.[77]

C. *The Fifth Amendment and Contractual Commitments*

In light of the Constitution's state-specific Contract Clause, the Fifth Amendment provides the prevailing legal framework for evaluating federal interference with existing contracts.[78] Contractual rights have long been

---

[70] *Id.* at 434–35.

[71] *Id.* at 447.

[72] *Id.* at 444–47.

[73] *See* Energy Reserves Group, Inc. v. Kan. Power & Light Co., 459 U.S. 400, 411–13 (1983).

[74] *Id.* As a general rule, a government action that affects only the remedy or the timing of payment fails to "substantially impair" a contract within the meaning of *Kansas Power*. *See* LEVY & MELLOR, *supra* note 49 at 51.

[75] Energy Reserves Group, Inc. v. Kan. Power & Light Co., 459 U.S. 400, 411–13 (1983). Note the similarity that this language has to the words "legitimate" and "compelling." Both describe governmental interests that justify interference with a fundamental right. Further similarities between Contract Clause jurisprudence and fundamental rights analyses are discussed *supra* Part II.C.2.

[76] *Id.*

[77] *Id.*

[78] U.S. CONST. amend. V. ("No person shall . . . be deprived of life, liberty, or property, without due process of law; nor shall private property be taken for public use, without just compensation.").

considered property rights for the purposes of the Fifth Amendment.[79] Under the Takings Clause of this Amendment, the federal government is prohibited from taking property from individuals for governmental use without compensation.[80] In contrast, the Due Process Clause protects individuals from depravation of property by the federal government without due process of law—regardless of whether the government is appropriating that property.[81]

1. *The Taking of a Contractual Right*

The government affects a constitutional "taking" of property only where it appropriates the value of an individual's property for government gain.[82] Contractual rights—whether exclusively bargained between private parties or whether the government itself is a party—are property under the meaning of the Fifth Amendment and are therefore protected by the Takings Clause.[83] Additionally, even if government action has helped to create the value contained in a particular property right, the government appropriation of that right still qualifies as a taking.[84] Perhaps because of the obvious injustice involved, few controversies involving the federal government's receipt of pecuniary benefits from voiding private contracts have survived settlement negotiations.[85] Given the clear cut nature of the underlying property right in a

---

[79] *See* Omnia Commercial Co. v. United States, 261 U.S. 502, 508 (1923).

[80] U.S. CONST. amend. V.

[81] *Id.*

[82] Penn Cent. Transp. Co. v. City of New York, 438 U.S. 104, 128 (1978).

[83] U.S. Trust Co. of N.Y. v. New Jersey, 431 U.S. 1, 19 n.16 (1977).

[84] Phillips v. Wash. Legal Found., 524 U.S. 156, 171 (1998). The *Phillips* Court took care to distinguish government appropriation of government aided value from permissible instances in which the government simply charges a reasonable fee for services rendered by the government. *Id.* The *Phillips* doctrine obviates the need to consider whether governmental stock purchases provided the capital from which TARP-regulated executive compensation was paid. Other aspects of TARP are considered against the Takings Clause *infra* Part III.

[85] *See* Merrill, *supra* note 48. Whether and in what circumstances TARP provisions could result in governmental profit at the expense of private contract will be discussed in greater detail in both Parts III & IV, *infra*. One such instance of federal appropriations of private rights could arise in the context of bank insolvency, leaving individuals left without recourse to recover contracted amounts while the government cashes out as much of its preferred stock as possible. A common misperception is that corporate bankruptcy might provide some justification for a government re-ordering of private debt. Though this may be true to some extent, even the federal power over bankruptcy is subject to the Fifth Amendment's Takings Clause. *See* United States v. Sec. Indus. Bank, 459 U.S. 70, 75 (1982).

contractual commitment, there is little reason to assume that governmental appropriation of private contractual rights would survive constitutional review.

2. *Property Deprivation and Due Process*

A very difficult question arises when examining whether a legislative action has deprived an individual of property without due process of law. On the one hand, *legislative action* is a traditionally accepted governmental procedure, and when such procedures are followed, economic legislation need only satisfy the rational basis test under ordinary due process conditions.[86] On the other hand, there are certain fundamental rights that are deemed so precious that the Due Process Clause acts by "barring certain government actions regardless of the fairness of the procedures used to implement them."[87] Although the right to enter into private contracts is no longer deemed fundamental,[88] the right to maintain property is specifically enumerated in the Fifth Amendment.[89] Fundamental rights cannot be abridged by the government without "compelling" justification using "narrowly drawn means."[90]

The Court's most noted treatment of contract impairment at the federal level, *Pension Benefit Guarantee Corp. v. R.A. Gray & Co.*, disclaimed any federal application of the Contract Clause and applied only the rational basis standard to the specific contractual impairment at issue.[91] But *Pension Benefit* did not address unilateral government interference into individual contractual relationships, but instead addressed the government's power to interfere with one private contract (embodied in a Collective Bargaining Agreement) in order to secure payments to a retirement account for pension benefits that had already vested for individual employees.[92] Viewed in that light, little is remarkable about the result in *Pension Benefit*, the Court simply weighed Congress' power to protect the implied contractual rights of

---

[86] *See* Gen. Motors Corp. v. Romein, 503 U.S. 181, 191 (1992).

[87] Daniels v. Williams, 474 U.S. 327, 331 (1986).

[88] W. Coast Hotel Co. v. Parrish, 300 U.S. 379, 392 (1937).

[89] U.S. CONST., amend V. Though much debate over current constitutional jurisprudence circles around what rights are deemed fundamental for the purposes of a due process analysis, it is generally accepted that rights enumerated by the Constitution receive this hallowed treatment. *See, e.g.*, United States v. Carolene Prods., 304 U.S. 144, 153 n.4 (1938).

[90] Bowers v. Hardwick, 478 U.S. 186, 189 (1986).

[91] 467 U.S. 717, 732–33 (1984).

[92] *Id.* at 734.

individual employees—as guaranteed under ERISA—from the reach of *ex parte* agreements among multiple companies and unions.[93]

Another interesting takeaway from *Pension Benefit* is the Court's unique application of the maxim that even economic legislation cannot be applied in an "arbitrary" or "irrational" way.[94] Though this initially provides no ground-breaking changes to the pre-supposed rational basis test, the opinion did include an additional step for retroactively applied legislation.[95] In order for economic legislation to pass constitutional muster when applied retrospectively—for instance, retrospective abrogation of contracts that predate the legislation—there must be a rational basis for applying the law retroactively.[96]

D. *The* Gold Clause Cases

The most dramatic foray into the federal impairment of contracts arose during the Great Depression when Congress enacted legislation to protect the nation's gold reserves.[97] During that period it was common practice for individuals to protect their pecuniary interest by inserting clauses into long-term contracts that allowed a party to demand payment on the contract in gold.[98] Such provisions were designed, in part, to protect against fluctuations in the value of currency, as the clauses specified an amount of gold—not the value of gold—to be paid.[99] The clauses were so widespread and legally accepted that long-term lease agreements often lacked annual rent escalations, opting instead for the inclusion of a "gold clause" provision to

---

93 *Id.* Because the Court only addressed the underlying claim under the standards reserved for economic legislation, it is difficult to say whether its Contract Clause disclaimer would apply with equal force if a true fundamental right to property were present.

94 *Id.* at 729–30 (quoting Usery v. Turner Elkhorn Mining Co., 428 U.S. 1, 15 (1976)).

95 *Id.*

96 *Pension Benefit Guar. Corp.*, 467 U.S. at 730. As later analysis will explain, the application of this secondary rational basis standard may be constitutionally relevant to retroactive provisions in the ARRA. *See infra* Part III.

97 *See* LEVY & MELLOR, *supra* note 49, at 51.

98 *Id.*

99 *Id.* As one might imagine, protection against inflation was at the forefront of the minds of many Americans during a time in which unemployment reached about twenty-five percent. *See* Franklin D. Roosevelt Presidential Library and Museum, How High Was Unemployment during the Great Depression?, *available at* http://www.fdrlibrary.marist.edu/unempl71.html (last visited Aug. 15, 2009).

protect against inflation.[100] Despite the prevalence of gold clauses, a string of executive and legislative actions resulted in the destruction of all such clauses.[101]

When the Supreme Court eventually decided the *Gold Clause Cases*, the Court barely touched upon the rights of the individuals affected and instead focused its analysis on congressional power to regulate the subject matter of the contracts.[102] The validity of the congressional abrogation of gold clauses turned upon a three part test.[103] First, does congressional power over currency include the power to control means of tender?[104] Next, if Congress can control the means of tender, does it have the power to invalidate existing contracts in conflict with statutory means?[105] Finally, do the contract provisions at issue conflict with congressional intent so that the provisions are void by statute?[106]

The answer to the first question proved quite easy, as historical precedent recognized that the congressional power to coin money included the power to prevent the "outflow" of the metals generally used to coin money.[107] The third question also provided little reason for pause, as Congress had expressly declared that gold could not be used as a medium of exchange.[108] The second question, however, directly addressed the point of conflict between the private contractual rights negotiated between individuals and the constitutional powers of the national legislature.[109]

The Court split the analysis in two, noting that contracts that involved the government must receive differing treatment from those involving only

---

[100] *See* LEVY & MELLOR, *supra* note 49, at 52. The cost of relying upon a gold clause for inflationary protection turned out to be enormous. One land owner who had used such a provision saw a rental increase from $23,000 per year to $460,000 per year when Congress amended the Depression-era legislation in 1993, more than sixty years after its enactment. *Id.*

[101] *See* Norman v. Balt. & Ohio R.R. Co., 294 U.S. 240, 316 (1935).

[102] *See* LEVY & MELLOR, *supra* note 49, at 51.

[103] *See Norman*, 294 U.S. at 302. The impetus behind presidential and congressional action that resulted in an abrogation of all gold clauses was defensible. Following the crash of the nation's stock markets and the economic disaster that followed, already depleted gold reserves were put in further jeopardy by individual citizens' demands for gold. *See* H. COMM. ON BANKING & CURRENCY, UNIFORM VALUE OF COINS AND CURRENCIES OF THE UNITED STATES, H.R. REP. NO. 73-169, at 1–2 (1933).

[104] *Norman*, 294 U.S. at 302.

[105] *See id.*

[106] *See id.*

[107] *Id.* at 304 (citing Ling Su Fan v. United States, 218 U.S. 302, 311 (1910)).

[108] *Norman*, 294 U.S. at 316.

[109] *Id.* at 307.

private parties.[110] But with respect to private contracts, parties received little sympathy from the Court: "Parties cannot remove their transactions from the reach of dominant constitutional power by making contracts about them."[111] The Court asserted that private parties negotiate with knowledge that Congress may someday choose to fully exercise its powers, thereby narrowing the scope of the potential provisions inherent to a given contract.[112] Furthermore, the Court reasoned, the overwhelming prevalence of existing gold clauses was so pervasive that the congressional goal of a uniform currency would be completely undermined if the clauses were not voided.[113] Perhaps most driven by this fear, the Court held gold clauses to be void because they interfered with the congressional power (previously unused) to establish a uniform currency.[114]

The *Gold Clause Cases* are important to the analysis of the executive compensation provisions of the Economic Stabilization Act in that they provide a distinct doctrinal framework for the evaluation of federal interference with contracts during economic emergency. This framework differs greatly from the three-part substantial impairment standard adopted in the context of Contract Clause analysis. The *Gold Clause Cases* also depart from the more familiar due process analysis in which contractual rights are recognized as constitutionally protected property rights.[115] Most importantly,

---

[110] *Id.* at 306. The Court handed down a decision on the same day that directly addressed the treatment of tender in gold when the government was a party to the questioned contract. *See* Perry v. United States, 294 U.S. 330 (1935) (though the Court recognized a limitation on congressional power to alter existing contracts to which the United States was a party, it still held that a change in the value of the nation's currency would not allow a private party to collect damages against the government even upon a contract that contemplated payment in gold).

[111] *Norman*, 294 U.S. at 308.

[112] *Id.* at 309.

[113] *Id.* at 312. What is particularly interesting about this rationale—especially in light of TARP's executive compensation provisions—is that the Court contrasted the 73d Congress's warranted justifications with the following: "If the gold clause applied to a very limited number of contracts and security issues, it would be a matter of no particular consequence." *Id.* The qualification seems relevant to TARP provisions that affect such high wage earners in a single industry and represent such a low percentage of the broader liquidity problem addressed by the Bill.

[114] *Id.* at 316. *Norman* stood the usual constitutional analysis on its head. Instead of considering whether a governmental exercise of power interfered with constitutionally protected rights (such as the property rights bestowed by contract), Chief Justice Hughes examined whether the exercise of individual rights interfered with an enumerated power of the federal government. *Id.* at 309.

[115] *See, e.g.*, Louisville Joint Stock Land Bank v. Radford, 295 U.S. 555 (1935). This case provides a particularly interesting contrast to the *Gold Clause Cases* as it was decided roughly five months after *Norman*.

the upside-down analysis used by the Court in these cases—examining whether the right claimed by the individual interfered with legitimate government power—represents a high water mark in fundamental rights review. As such, any contractual impairment that fails the government-friendly *Gold Clause Cases'* analysis would likely fail to satisfy *any* constitutional standard.

III. THE CONSTITUTIONAL LIMITATIONS FOR EXECUTIVE COMPENSATION REGULATION

What most complicates the legal assessment of TARP's executive compensation provisions is not just that there are several constitutional lenses through which they could be examined. The regulatory scheme creates a plethora of overlapping applications, and the timing and amount of government investment is determinative of which limits apply to which executives.[116] For the purposes of orderly analysis, it is useful to first separate TARP's restrictions into two categories. The first category is made up of the restrictions that TARP places upon the payment of golden parachute clauses. The second category is comprised of the restrictions that TARP places on the salary and bonuses paid to executives by funded institutions. The two groups of restrictions are considered below.

A. *The Constitutionality of Golden Parachute Restrictions*

The restrictions on golden parachute payments contained in the original EESA applied only to the compensation of "the top 5 highly paid executives of a public company."[117] But the limitation was extended to cover the senior

---

[116] EESA § 111. Provisions contained in § 111 of the EESA prohibiting golden parachute payments if certain criteria are met apply to all companies that have received TARP funding. Additional restrictions are included on most assets through regulation. *See* 31 C.F.R. § 30 (2008). Many of these restrictions may be somewhat insulated from legal attack by waivers of claims signed by the Senior Executive Officers of funded institutions pursuant to the terms of the funding agreements. *See, e.g.*, Securities Purchase Agreement § 1.2(d)(v), *supra* note 15. The amount of the subsequent regulation arguably provides a change of circumstance under which the waivers are not enforceable. After all, banks receiving aid after February 4, 2009, are subject to the tiered executive compensation limitation imposed by President Obama's administration. *See* TG-15, *supra* note 26. All banks who have received any aid are subject both prospectively and retrospectively to the bonus restrictions attached to the 2009 stimulus bill. *See* ARRA § 7001. Depending upon the amount of federal investment, the number of executives who face those bonus restrictions may be one, five, fifteen, or twenty-five. *Id.* Finally, funded institutions that entered into employment contracts with top talent following February 11, 2009, are subject to further statutory limitations. *Id.*

[117] EESA § 111(b)(3).

executive officer and the "next 5 most highly compensated employees," putting an additional employee at each funded institution under the golden parachute restrictions.[118] Even after the subsequent legislative refinement of the restrictions, some difficulty lies in determining how long and with what force the golden parachute restrictions apply.[119] Even more uncertainty exists in determining what the potential implications are for denying such a payment, as the act does not specifically establish penalties.[120]

There are a couple of avenues down which questions concerning the constitutional viability of golden parachute restrictions might arise. In fact, considering the nature of a golden parachute and the condition of the institutions in which the Secretary is investing, it seems nearly certain that the clauses themselves will be triggered in at least a few contracts.[121] For one, because Congress has so broadly defined "golden parachutes," the statute may prohibit making *any* severance payment to covered executives.[122] But an even more likely trigger exists, as one would expect massive control changes, involuntary terminations, and bankruptcies in an industry driven to the brink of collapse by poor management and bad economics.[123]

Given the enormous monetary value of top executives' pre-negotiated severance packages, one might doubt that goodwill and public image concerns would cause any ousted executive to walk away quietly without

---

[118] ARRA § 7001(b)(3)(c) (amending EESA § 111).

[119] Though the Act includes a sunset provision limiting the authority of the Secretary of Treasury to purchase assets outside of a given time frame, the Act specifically exempts the Secretary from the sunset provision with respect to holding assets purchased before the provision runs. EESA § 106(e).

[120] One possible theory is that the government could sue a disobedient bank for breach of contract. Such a claim would be a difficult sell, however. Many of the legal restrictions were added after the preferred stock agreements were executed. These administrative uncertainties are addressed more fully *infra* Part IV.A.

[121] Though the traditional golden parachute clause is triggered only when there is a change in control of the corporation—thereby providing perceived protection for executives in the event of a hostile takeover—conversational parlance has expanded the definition to include a much broader range of severance packages. The EESA appeared to contemplate a broad definition of "golden parachute," as it restricted firms from contracting for "a golden parachute in the event of an involuntary termination, bankruptcy filing, insolvency, or receivership." EESA § 111(c). Congress confirmed this broad reading in February 2009 by defining a golden parachute as "any payment to a senior executive officer for departure from a company for any reason." ARRA § 7001(a)(2) (amending EESA § 111(a)(2)).

[122] *Id.*

[123] Indeed, while this Note was being written, John Thain was forced out of Bank of America for his (mis)management of Merrill Lynch during Bank of America's takeover of the brokerage giant. *See* Julie Creswell & Joseph Story, *A Charmed Wall Street Career Is Derailed at Bank of America*, N.Y. TIMES, Jan. 23, 2009, at A1.

receiving the negotiated package.[124] When the time comes that an executive does challenge TARP for depriving her of a contractually negotiated property right, the defensibility of the Act will turn upon both the construction of the Act and which constitutional framework the reviewing court chooses to apply. The entire controversy, in fact, might hinge upon two questions: (1) How much does TARP interfere with the contractual property rights of the ousted executive officer? and (2) Is Congress's constitutional authority broad enough to so interfere?

Because the first question will be a function of statutory construction, ongoing Treasury regulation, and a case-by-case negotiation between the Treasury and troubled banks, this Note does not attempt to definitively answer it.[125] Instead, the following subsections examine the question in light of three hypothetical constructions of the golden parachute prohibition.[126] First is an explanation of the constitutional implications if the statute is read

---

[124] The sheer size of corporate severance packages would demand action from any individual who was denied such payment. Of course, the bogey-man story of these packages might be the $210 million dollar parting gift reportedly given to Robert Nardelli upon his ouster from Home Depot—and the resulting media and public outcry. *See Golden Parachutes of the Past Year: Robert L. Nardelli*, BUS. WK., http://images.businessweek.com/ss/06/12/1222_golden_parachute/source/8.htm (last visited Jan. 13, 2009). But even John Thain's predecessor at Merrill Lynch received a $160 million parting gift for his time at the helm. *See* Pallavi Gogoi, *Thain Resigns from Bank of America After News of Bonuses*, USA TODAY (Jan. 22, 2009). One interesting development in light of golden parachute prohibitions is the potential proliferation of voluntary retirement. As this Note goes to press, Ken Lewis is prepping for retirement from his post as CEO of Bank of America. *See* Hibah Yousuf, *No 2009 Pay for Bank of America CEO Ken Lewis*, CNN, Oct. 16, 2009, http://money.cnn.com/2009/10/15/news/companies/bofa_lewis_salary/index.htm?postversion=2009101614. Possibly in anticipation of a fight over his $53 million retirement package and $69 million total payout after calculating the value of accompanying stock options, Lewis struck a deal with so-called "pay czar" Kenneth Feinberg that has Lewis repaying Bank of America all of his salary and bonuses for 2009. *See id.*

[125] One need only look to the importance of characterizing John Thain's departure from Merrill Lynch as a termination, as opposed to characterizing Ken Lewis's departure as voluntary, to see some of the potential iterations of forthcoming battles over golden parachutes. *See* discussion *supra* notes 123–24. Though this Note does not attempt to define the boundaries of these potential skirmishes, Parts III.A.1–3, *infra*, do present plausible predictions about the extent to which TARP will interfere with private contractual rights.

[126] Many more issues are presented when considering the potential implications of golden parachute packages that are contractually interwoven with more traditional retirement and health care benefits. It is difficult to imagine that either the EESA or the ARRA target any of these types of benefits, but it is equally difficult to predict how to unwind only the targeted perquisites in order to effectively administer the statute. Some of these issues of administration will be explored more fully in Part IV, *infra*.

to simply delay golden parachute payments for a reasonably ascertainable period of time, eventual payment being a certainty on the horizon. Next follows a discussion of the implications if the statute delays payment indefinitely with the likelihood—but without the guaranty—of eventual payment. Finally, there is a discussion about what would happen if the statute has the effect of destroying all contractual obligations with respect to the effected clauses.

1. *Revisiting* Blaisdell*: "Moratoria" on Golden Parachute Payments*

Though a temporary delay in the *tender* of golden parachute payments is not without difficulty, such a construction of the EESA's provisions would likely pass constitutional muster. The threshold requirement for an individual to sustain a claim based upon the impairment of contract rights is that a contract was "substantially impaired."[127] As long as the government acts only to delay the remedy for a contractual commitment, and not destroy the contractual obligation, no substantial impairment exists and the corresponding legislation need only be reasonably related to the legitimate purpose that prompted the action.[128] In light of this requirement, it seems unlikely that TARP's golden parachute restrictions violate the Constitution, if golden parachute payment is merely delayed until after the Treasury's shares are redeemed, as opposed to an interpretation that entirely voids the golden parachute.[129]

---

[127] *See* Energy Reserves Group v. Kan. Power & Light, 459 U.S. 400, 411–13 (1983). Note that some contract cases—such as one where no property right is actually destroyed—are treated as coextensive with general economic legislation, warranting only rational basis review. *See* Pension Benefit Guar. Corp. v. R.A. Gray & Co., 467 U.S. 717 (1984). It bears mentioning, as well, that the Contract Clause is probably at least as protective of a contractual property right as federal (fundamental rights) due process would be. Because Contract Clause doctrine acknowledges the government's power to define contractual rights (i.e. to remedies) as being coextensive with its power to impair contracts, *see* Home Bldg. & Loan Ass'n v. Blaisdell, 290 U.S. 398, 444–47 (1934), it follows that a fundamental contractual right would be limited by the same governmental power to define the contractual rights. Therefore, finding the EESA acceptable under a Contract Clause analysis obviates the need to conduct a fundamental rights analysis, which would be couched in the language of addressing a "compelling interest" using "narrowly tailored means."

[128] *Blaisdell*, 290 U.S. at 444–47.

[129] This approach finds further support in the jurisprudence connected to "regulatory" takings. *See* Tahoe-Sierra Pres. Council, Inc. v. Tahoe Reg'l Planning Agency, 535 U.S. 302, 341–42 (2002) (upholding a local multi-year moratorium on land development, in part, because the attendant delay of the land-owner's realization of the property's economic value was temporary).

Even if a delay in the payment of a golden parachute becomes lengthy, the feared crash of our nation's entire financial system is arguably a sufficient emergency to justify a temporary impairment.[130] Additionally, one of the EESA's secondary purposes—protecting taxpayers' investments—provides more justification for upholding measurably finite contract impairment.[131] As a preferred stockholder, the Treasury's liquidation preference in bankruptcy would be subordinate to that of many others, including unpaid CEOs.[132] It is an obvious benefit to taxpayers to minimize the number of expenses that must be paid before the Treasury is repaid. Although this justification faces some criticism as being too small to have real impact, taxpayer protection is directly addressed, and there are few strong countervailing interests if executives will eventually be paid the value of their contracts—absent bankruptcy.[133] The federal interest is strengthened by the fact that company executives have a strong incentive to repay taxpayers quickly in order to reap the value of their contractual rights more quickly.[134] In sum, if golden parachute legislation simply delays the payment of the provisions, the restrictions are constitutionally permissible.[135]

---

[130] Recall that a Minnesota statute lengthening the term of mortgage agreements, many of which already extend for years, was held to be acceptable given the important interest of preserving housing for the states' beleaguered residents. *See Blaisdell*, 290 U.S. at 444–47. Preventing the crash of the nation's financial system would have a much broader impact. Of course, the golden parachute restrictions do not aim to preserve the viability of our nation's economy; they are simply part of a larger scheme to address that problem. As is often the case, the constitutional outcome of this issue may depend entirely upon how a court frames the problem.

[131] *See* EESA § 103(1) (establishing taxpayer protection as one of the key purposes of the Act). The importance of this purpose of the Act, as measured against the Act's other purposes, is considered in greater detail *infra* Part IV.

[132] Outstanding obligations to employees are considered unsecured debt and remain senior to any equity interests should the firm dissolve in insolvency or go through a bankruptcy reorganization or liquidation. *See* 11 U.S.C. § 726(a)(1) (2006).

[133] The balance may strike quite differently if circumstances were such to permanently deprive covered executives of their contractual payments.

[134] No such incentive would exist if repayment would not revive the golden parachute debt. Whether this incentive is actually a positive policy goal for the TARP program will be debated *infra* Part IV.

[135] It is beyond the scope of this Note to address the potential implications of an indefinite delay in the payment of a golden parachute clause. The Court has yet to address such a case in the context of contractual rights. On the one hand, the reasoning of *Blaisdell* suggests that any delay in remedy may be acceptable. *See* 290 U.S. at 444–47. On the other hand, at some point the delay could become so long as to effectively destroy the obligation—such as if the employer filed for bankruptcy prior to paying out the contractual debt. Even within bankruptcy, however, there are two potential circumstances that could prompt different legal analysis. The first instance would occur in a bankruptcy

2. *At What Point Would TARP's Restrictions Amount to a Taking?*

For the sake of brevity and clarity, this Note examines only bankruptcy as a potential, and not so unlikely, trigger for a potential takings claim with respect to golden parachute restrictions.[136] For a takings claim, it's not the destruction of the obligation by itself that implicates the Takings Clause; the Clause is only implicated when the government is the beneficiary of the destruction.[137] In other words, the golden parachute restrictions only affect an unconstitutional taking if the government is the beneficiary of the very thing that is being withheld from the individual.

Without § 111 of the EESA, a bankruptcy filing would ensure that a terminated executive officer (as a creditor of the bank) would receive an equitable portion of the money for which she contracted—prior to all equity holders (such as the Treasury Department).[138] With § 111, the officer cannot be paid until the Treasury Department's shares have been redeemed.[139] If Citibank, for instance, had filed for bankruptcy in November of 2008, the Treasury would have been entitled to receive $25 billion before the company's top five executive officers received any of their agreed-upon severance.[140] Other creditors of the firm, including ex-employees with whom the firm had contracted for severance payments, would receive their money prior to the government, but top executives could potentially watch as the government cashes their checks. Because bankruptcy does not exempt the government from the Takings Clause,[141] the re-ordering of debt to the advantage of the government would constitute impermissible government action.

---

proceeding after which neither the Treasury nor the senior executives received their respective pay-outs. In this instance, due process and the fundamental right to contractual property provides the proper analytical framework. The second instance would come to pass if the firm had enough assets to satisfy the outstanding obligation to the government, but not to the executive officers. This circumstance has the potential to seriously implicate the Takings Clause of the Fifth Amendment. *See infra* Part III A.2.

[136] In fact, as late as mid-February 2009, analysts were estimating that the entire U.S. banking system was insolvent in the aggregate—even after receiving TARP funding. *See* Nouriel Roubini, *Dr. Doom: Nationalize Insolvent Banks*, FORBES.COM, Feb. 12, 2009, http://www.forbes.com/2009/02/11/geithner-banks-nationalization-opinions-columnists_0212_nouriel_roubini.html. With the entire industry in such dire straits, individual bankruptcies seem nearly inevitable.

[137] *See supra* Part II.C.1.

[138] *See* 11 U.S.C. § 726(a)(1) (2006).

[139] ARRA § 7001(b)(3)(D)(i) (amending EESA § 111(b)(1)).

[140] *See* Mary Snow, *Where's the Bank Bail Out Money?*, CNN, Dec. 23, 2008, http://www.cnn.com/2008/US/12/22/bailout.accountability/.

[141] *See* United States v. Sec. Indus. Bank, 459 U.S. 70, 75 (1982).

3. *Will Golden Parachutes Be Grounded for Good?*

There is another potential, and ominous, result of the amalgam of golden parachute restrictions. It involves the complete destruction of any rights negotiated under a golden parachute clause. Unless the government itself was the beneficiary of such a broad reading, there would not be a colorable issue with respect to the Takings Clause.[142] However, there seems to be something intuitively unfair about the government unilaterally abrogating the existing contracts of particular individuals.[143] Property rights such as this one may indeed be so fundamental as to invoke a controversial fundamental rights review under the Due Process Clause of the Fifth Amendment.[144]

Under the analogous *Blaisdell* analysis, the complete abrogation of a contract's benefits would almost certainly affect a substantial impairment of a contract.[145] And though the government has a legitimate explanation for delaying the negotiated benefits, there is less justification for absolutely destroying the payment rights embodied in a golden parachute clause, particularly if that destruction persists after the Treasury's shares have been redeemed.[146] But a question still remains as to whether the broad federal powers suggested by the *Gold Clause Cases* might subsume the contractually negotiated golden parachute rights.[147]

Much like in the *Gold Clause Cases*, the broad purpose of the TARP program is to stabilize the financial markets.[148] At least derivatively,

---

[142] *See supra* Part III.A.2.

[143] One might go as far as to suggest that singling out the top five executives for the punitive treatment of abrogating their contracts amounts to a bill of attainder. Though the specificity test for such bills may be a difficult sell, it bears mentioning that the retrospective application of this law bears a resemblance to at least a handful of laws that have been appraised as Bills of Attainder. *Compare* United States v. Lovett, 328 U.S. 303 (1946) (holding that legislative action that denied three named individuals their salaries was sufficiently similar to punishment to qualify as a Bill of Attainder), *and* United States v. Brown, 381 U.S. 437 (1965) (voiding a statute making it a crime for a member of the Communist party to hold a union position), *with* Bd. of Governors of the Fed. Reserve Sys. v. Agnew, 329 U.S. 441 (1947) (upholding a statute that forbade employees of securities underwriters from holding a director's position at a bank).

[144] *See* Merrill, *supra* note 48.

[145] *See* Energy Reserves Group v. Kan. Power & Light, 459 U.S. 400, 411–13 (1983). Recall also that the Contract Clause jurisprudence offers acceptable parallels to fundamental rights Due Process. *See* discussion *supra* note 127.

[146] Though prohibiting golden parachute payments in the near-term could enhance the likelihood of recouping taxpayer investment, a key purpose of the EESA, that justification evaporates once the investment has been recouped.

[147] *See* discussion *supra* note 114.

[148] *See* EESA § 2(1).

Congress has acted to stabilize the nation's currency,[149] and the power to regulate currency is the very power protected by the *Gold Clause Cases*.[150] But in the *Gold Clause Cases*, the contractual right at issue was itself at odds with congressional power to establish a uniform currency as the nation's medium of exchange.[151] Present-day Congress did not choose to limit golden parachute clauses in order to protect the national currency; Congress chose to invest in troubled banks to increase financial liquidity with the potential side effect of protecting the value of the nation's currency.[152] The restrictions placed upon golden parachute clauses are more aptly described as a protection of taxpayer investment.[153] Though this is a laudable goal, it hardly warrants the upside-down analysis put forward by Chief Justice Hughes in *Norman*.[154] Absent the *Gold Clause Cases'* narrow view of constitutional rights, a complete abrogation of a golden parachute clause would violate due

---

[149] Since abandoning the gold standard, the value of the nation's currency has been mostly controlled through market mechanisms. The primary mechanisms of control have included buying and selling Treasury Securities for U.S. dollars, adjusting the interest rate that the Federal Reserve Bank charges member institutions for short term lending, and manipulating the reserve requirements for federally insured banks. THE FEDERAL RESERVE SYSTEM, PURPOSES AND FUNCTIONS 3 (2005), *available at* http://www.federalreserve.gov/pf/pdf/pf_1.pdf. Any great shock to the private market in which the Federal Reserve operates could arguably have a tremendous impact on the effectiveness of the policy, thereby affecting the underlying value of United States currency.

[150] *See* Norman v. Balt. & Ohio R.R. Co., 294 U.S. 240, 316 (1934).

[151] *Id.*

[152] *See* EESA § 2(1).

[153] EESA § 2(2)(C). Of course, given the comparative difference between the tens of billions of dollars of bank investments and the hundreds of millions of dollars of golden parachute obligations, the amount of taxpayer-protection provided by golden parachute restrictions is too small to have any real effect on a TARP supported firm's ability to redeem the Treasury's shares.

[154] *See supra* note 114 for discussion. Likewise, it cannot be gainsaid that the Congress's broad spending powers offer any more justification for interfering with the contractual rights of individuals to whom Congress is not giving money. It is necessary to be aware of an important analytical distinction: between permissible congressional control over the banking institutions to which Congress has provided money, and the less defensible governmental control over the employees to whom Congress has provided nothing. It is quite possible that Congress can, by invoking its spending power, prohibit a banking institution from making payments to executives, but that this prohibition would not protect the banking institution from contractual liability to the same executives. Although in a different context, *NCAA v. Tarkanian* offers some insight into the Court's position on an entity's duty to comply with conflicting agreements. 488 U.S. 179 (1988) (reasoning that the University of Nevada, Las Vegas was not relieved of its contractual obligations to basketball coach Jerry Tarkanian when the NCAA issued a mandate that the university terminate the coach's employment).

process.[155] Any construction of TARP's restrictions that would produce such a result would be constitutionally invalid.

B. *The Constitutional Implications of Salary & Bonus Limits*

The complexity of rules governing executive compensation—other than those governing the previously discussed golden parachute clauses—creates the need for a highly contextual analysis. Given the ever changing composition of the list of funded institutions—and the ever changing composition of government-imposed restrictions—it is unclear exactly how many institutions and executives will fall under both legislative and executive guidelines.[156] Congress' eleventh-hour addition to the stimulus bill bestows broad authority—maybe even a mandate—on the Secretary of Treasury to apply statutory restrictions retroactively to compensation paid before the most recent legislative directive.[157] The constitutional posture with respect to individual banking institutions will depend in part upon whether both sets of limitations apply to that bank. Additionally, two distinct classes of guidelines exist, each with its own implications: (1) The guidelines that have only prospective applicability produce only a narrow band of constitutional concern; and (2) The guidelines with retroactive applicability

---

155 *See supra* note 135 and accompanying discussion.

156 Recall that President Obama and Secretary Geithner proposed a prospective restriction on executive compensation for banks receiving additional TARP funds after February of 2009. *See* TG-15, *supra* note 26. These restrictions would have capped salary for certain executives, and allowed for unlimited bonus payments as long as the bonuses were paid in deferred stock only. *Id.* Less than two weeks later, Congress allowed for unlimited salary payments, but retroactively capped bonus payments to one-third the amount of yearly salary. ARRA § 7001 (amending EESA § 111(b)(3)(D)(i)(II)). Some time later, the Obama administration abandoned its plans to enforce a blanket cap on the salaries of executives, and instead the President moved to entrust a special master of compensation, or pay czar, with the authority to regulate the compensation of the top 100 wage earners at certain TARP-supported institutions. *See* Deborah Solomon, *Pay Czar Gets Broad Authority over Executive Compensation*, WALL ST. J., June 11, 2009, http://online.wsj.com/article/SB124464909136002467.html. The matter is further complicated by the growing group of institutions that has redeemed the Treasury's investment, a group that notably includes Goldman Sachs as well as several regional banks. *See* OFFICE OF FIN. STABILITY, U.S. TREASURY DEP'T, CUMULATIVE DIVIDENDS REPORT (Oct. 21, 2009), *available at* http://www.financialstability.gov/ docs/dividends-interest-reports/August2009_DividendsInterestReport.pdf.

157 ARRA § 7001 (amending EESA § 111(f)(2)). Pay czar Kenneth Feinberg has publicly proclaimed his intention to exercise this broad authority to clawback amounts paid out to executives wherever he finds "an egregious fact pattern" that would warrant a clawback. *See* Karey Wutkowski, *Pay Czar Emphasizes Wide "Clawback" Power*, ABC NEWS, Oct. 23, 2009, http://abcnews.go.com/Business/wireStory?id=8901823#.

which produce a much broader array of constitutional problems. Each set of guidelines are considered below.

1. *Constitutional Hurdles for Prospective Guidelines*

Most of the restrictions embodied in either executive guidelines or statute present little cause for constitutional concern if applied only prospectively. Unlike the blanket treatment contemplated for golden parachute payments, Congress' strictest rules with respect to salary and bonuses do not apply if covered executives have contractual rights protecting those payments.[158] Likewise, even early restrictions contemplated by President Obama and Secretary Geithner did not seek to limit the amount of payment available to executives, but instead sought to regulate the form the payment would take.[159] But a problem arose when the statutory and regulatory restrictions overlapped to limit both the amount of salary-compensation and the amount of bonus-compensation.[160]

The mechanics of the conflict may be somewhat difficult to understand. The regulatory restrictions supplied a hard cap for the salaries of covered executives.[161] The effects of the cap would have been mitigated by allowing unlimited performance bonuses so that the underlying pecuniary obligations of the contract could be preserved.[162] But the statutory restrictions limit bonuses to an amount that cannot exceed one-third of a covered executive's total salary.[163] Because the statute excludes bonuses secured by contract,

---

[158] *Id.* (amending EESA § 111 (b)(3)(D)(iii)) ("The prohibition required under clause (i) shall not be construed to prohibit any bonus payment required to be paid pursuant to a written employment contract executed on or before February 11, 2009.").

[159] *See* TG-15, *supra* note 26. Though some argument could be made against requiring executives to change a portion of their total compensation from salary to performance bonus, the technical nature of that argument is beyond the scope of this Note. For the purposes of present discussion, assume that the change in the structure of an executive's compensation qualifies as a characterization of remedy and not a destruction of the underlying obligation. *See* discussion *supra* Part III.A.1.

[160] Though this interaction does create serious concerns, the pervasiveness of the problem should not be overstated. The bulk of the regulatory restrictions proposed by President Obama and Secretary Geithner apply only to institutions receiving *new* funding. *See* TG-15, *supra* note 26. The strictest of the Treasury rules apply only to banks receiving "exceptional" assistance, reducing even further the potential effects. *Id.* Still, the fervor with which Kenneth Feinberg has vowed to perform his duties suggests that the small number of conflicts that will erupt concerning compensation could prove to be epic battles. *See* Wutkowski, *supra* note 157.

[161] *See* TG-15, *supra* note 26.

[162] *See id.*

[163] ARRA § 7001 (amending EESA § 111(b)(3)(D)(i)(II)).

contracts that were formally altered following the issuance of regulatory direction could have become exempt from the latter restriction.[164] But two factors combined to reduce the protection of the exclusion clause. First, the statute only protects contracts entered into prior to February 11, 2009[165]—a date only seven days after President Obama and Secretary Geithner announced their restrictions.[166] Very few, if any, funded institutions had enough time to formalize changes in compensation structure to reflect the regulatory changes. Once the seven day window between the two guidelines closed, the statutory bonus restriction acted as an absolute bar to supplementing salary with bonus in order to reduce the pecuniary effects of the Treasury-imposed salary cap.[167]

Where the Treasury direction overlapped, and even conflicted, with the statutory scheme, a large constitutional question emerged. Funded institutions could not substitute performance bonuses to cover what might amount to large reductions in salary as a result of the regulatory interplay.[168] The result was the total destruction of a contractual right to the portion of the salary that is not recoverable.[169]

Such a result placed portions of the early 2009 regulatory regime outside the contemplation of Supreme Court precedent concerning the mere adjustment of contractual remedies.[170] Notwithstanding that some level of heightened scrutiny should apply to the destruction of a constitutionally enumerated property right, the piece-meal, maladroit operation of the conflicting policies may have failed to survive even rational basis scrutiny. While the Treasury may indeed have a rational basis for preferring

---

[164] *See id.* (amending EESA § 111(b)(3)(D)(iii)).

[165] *Id.*

[166] *See* TG-15, *supra* note 26.

[167] In actuality, many institutions may opt to drastically increase executive salaries—prior to or instead of requesting more funding—in order to avoid or mitigate the oppressive bonus restrictions. This, of course, directly contravenes the policy pursued by the Treasury in promulgating the salary cap. The wisdom and viability of these conflicting administrative and economic incentives will be discussed more thoroughly *infra* Part IV.

[168] For instance, Ken Lewis of Bank of America received an annual salary of $1.5 million in 2008. *See CEO Compensation*, FORBES.COM, Apr. 30, 2008, http://www.forbes.com/lists/2008/12/lead_bestbosses08_Kenneth-D-Lewis_PAU6.html.

[169] In the case of Ken Lewis, the destroyed obligation would have been $1 million. *See id.* The unintended interaction between Treasury-imposed salary limits and legislatively mandated bonus restrictions may have prompted the administration to abandon its hard cap on salaries. *See* Solomon, *supra* note 156.

[170] *See Blaisdell*, 290 U.S. 434–35, 447 (reasoning that governmental power to prescribe contractual remedies justifies government action where the underlying obligation is not destroyed).

performance bonuses over salary, and Congress may have a rational basis for preferring salary over bonuses, the two policies do not rationally coexist.[171] The Treasury consciously declined to place any limit on the amount of bonuses each firm could pay.[172] Congress declined to place any restriction on the amount of salary each firm could pay.[173] Both designed restrictions to avoid the absolute destruction of contractual rights, but the combined result is that some executives would have been precluded from recovering a substantial portion of their contractual salary. Perhaps because of this harsh result, the Treasury Department abandoned its capped-salary approach opting instead for a case by case examination of each bank's compensation. The new focus avoided the constitutional hurdle presented by conflicting executive and legislative policy, but the approach ran head on into a constitutional wall when the administration began looking to take back money already paid to executives in satisfaction of the executives' contractual rights.

2. *The Ominous Effects of Retrospective Regulation*

Whereas the prospective application of the regulatory regime produced only a narrow band of constitutional concerns, the retrospective aspects of the restrictions now trumpeted by so-called pay czar Kenneth Feinberg create a greater range of problems, many of which are beyond the scope of this Note.[174] The major facet of the law's retroactive application that this Note

---

[171] The result might be somewhat different if either the Treasury or Congress had acted to create an integrated scheme restricting both salary and bonuses.

[172] *See* TG-15, *supra* note 26.

[173] *See* ARRA § 7001. It can hardly be said that Congress did not consider whether salary restrictions were appropriate, Senator McCaskill's bill to explicitly limit executive salaries had been introduced, but not passed, just weeks earlier. *Angry Senator*, *supra* note 24. This is not to say that Congress has been entirely passive concerning high salaries. The Internal Revenue Code has historically limited the amount of an individual's salary that a company can deduct from income for tax purposes. *See* 26 U.S.C. § 162(a)(1) (limiting a business's deduction to "a reasonable allowance for salaries or other compensation for personal services actually rendered"); *see also* 26 U.S.C. § 162(m)(1) ("In the case of any publicly held corporation, no deduction shall be allowed under this chapter for applicable employee remuneration with respect to any covered employee to the extent that the amount of such remuneration for the taxable year with respect to such employee exceeds $1,000,000.").

[174] *See* Wutkowski, *supra* note 157. Feinberg's focus on clawbacks from individuals are well within the scope of this Note, but another portion of ARRA applies salary and bonus restrictions to financial institutions that received funding—with attendant contractual guarantees in the form of a preferred shares agreement—prior to the enactment of the restrictions. ARRA § 7001 (amending EESA § 111(b)(1)). To the extent that the statutory restrictions are inconsistent with the pre-existing securities agreements,

will address concerns the clawback of bonuses that have already been paid.[175]

The enacted language requires the Secretary of Treasury to review "prior payments" made to "the senior executive officers and the next 20 most highly-compensated employees of each entity receiving TARP assistance *before* the date of enactment," to ensure that those payments do not conflict with the Act's provisions.[176] The Treasury's review is not limited by the language of the statute, but can extend to ensure that prior payments are consistent "with the purposes of this section or the TARP . . . [and not] otherwise contrary to the public interest."[177] Most shockingly, payments that fail inspection are to be reimbursed to the federal government, not to the financial institution that paid the bonuses.[178]

Assuming for the purposes of initial discussion that clawback payments will not go to the government, the retroactive nature of the law may still unconstitutionally interfere with executive officers' property rights. First of all, both cash and stock (either might be relevant, depending upon how the reviewed bonuses were paid) are undoubtedly property within the meaning of the Fifth Amendment, and as such the holder of cash and stock is at least entitled to due process before forfeiting the property.[179] Furthermore, most of the affected payments were not made pursuant to illegal contractual provisions, as some were made prior to the enactment of the law that purported to prohibit them and others were made following the enactment of the law while no specific prohibitions existed to limit such payments. Considering the legitimacy of the executives' property rights, any destruction

---

the inconsistencies will be subject to a heightened level of scrutiny appropriate for the governmental regulation of its own contracts. *See generally* Perry v. United States, 294 U.S. 330 (1935). Though it presents an interesting discussion, the complex jurisprudence concerning statutory alteration of the so-called public contract is beyond the scope of this Note.

[175] ARRA § 7001 (amending EESA § 111(f)).

[176] *Id.* (emphasis added).

[177] *Id.* Given the current administration's hesitance to join Congress's jaunt into corporate governance, this provision will likely have little practical effect. With that said, providing such broad agency discretion to unilaterally confiscate money from private individuals nearly shocks the conscience.

[178] *Id.* One doubts that the Framers of the Constitution would have approved of the federal government taking possession of monies in private hands because a government official believed seizure to simply be in the "public interest." Whether anyone in the administration intends to require that clawback payments be made directly to the Treasury, as provided by the statute, is not clear. There is no indication, for instance, that Ken Lewis's 2009 salary was repaid to the Treasury. *See* Yousuf, *supra* note 124.

[179] *See* Merrill, *supra* note 48. Even if the payments were made in the form of stock, they would still undoubtedly be property under all constitutional definitions. *See id.*

of those rights should be subjected to a heightened scrutiny befitting a fundamental right.[180]

But matters are further complicated by statutory language that allows the Treasury to directly seize money paid by banks to individual executives.[181] If the statute is enforced as written, the government faces a logical quandary that almost certainly results in a violation of the Takings Clause of the Fifth Amendment.[182] On the one hand, the Treasury could argue that the payments made to executives were in violation of law and public policy and could be rescinded.[183] But this argument does not explain why the payments would go to the Treasury; it simply offers a theory through which the funded institutions could recover the payments. On the other hand, Treasury could defend itself against a *funded institution*'s takings claim by discounting the outstanding balance of preferred shares by an amount equal to the recovered amount.[184] But this argument fails to provide any remedy for *individual executives* who are forced to refund portions of their bonuses. In substance the entire process boils down to the government seizing property—specifically cash—that legally belonged to individual citizens in good standing with the law. This appropriation of private rights for the public good is, by definition, an unconstitutional taking.[185]

Many of TARP's restrictions on executive compensation run dangerously close to impinging upon constitutionally protected private rights,[186] but the retroactive application of bonus restrictions almost undoubtedly crosses the line. Clawing back compensation for government use pursuant retroactive legislation surely runs afoul of the Takings Clause. Unlike restrictions upon golden parachute payments, clawbacks are not indirect routes to ensure prompt redemption of Treasury-held shares.[187] In contrast to prospective limitations on salary and bonuses, clawbacks take away from individuals not only accrued *rights* but also *actual property* that is

---

[180] This analysis could differ greatly from the legal analyses employed to evaluate most contractual impediments. Unlike the expectancy of value contained in a contractual right, affected executives are currently in *possession* of the consideration the government wishes to rescind. For an in depth discussion of the many faces of constitutional property, *see* Merrill, *supra* note 48.

[181] ARRA § 7001 (amending EESA § 111 (f)).

[182] *See supra* Part III.A.2.

[183] Even this argument has dubious dimensions. *See supra* notes 174–78 and accompanying discussion.

[184] *See* Penn. Cent. Transp. Co. v. City of New York, 438 U.S. 104, 107 (1978) (providing "just compensation" for the property that was seized).

[185] *See id.*

[186] *See supra* Parts III.A, B.1.

[187] *See supra* Part III.A for discussion concerning golden parachutes.

in the possession of citizens.[188] In other words, clawbacks share many negative hallmarks with TARP's other restrictions, but fail to have any of the redeeming qualities.[189]

IV. THE ADMINISTRATIVE AND ECONOMIC PITFALLS OF COMPENSATION LIMITS

Unlike the constitutional problems for various executive compensation limits imposed by statute and executive action, some broader economic costs have received attention in the popular press and among financial analysts. For purposes of analysis, these costs will be considered separately in two categories: (1) administrative, including monitoring and enforcement, costs; and (2) economic loss, including those likely losses caused by poorly aligned incentives.

A. *Administering a Complex Regulatory Scheme*

As of February 14, 2009, there were 359 banks that had received some financial assistance from the Treasury Department, and by July that number had grown to 651.[190] Of these, the investment amounts in each bank ranged between $1 million and $50 billion.[191] Though the actual number of employees covered by various TARP-related restrictions on compensation depends upon the timing and amount of each institution's receipt of funds, even approximate figures are staggering. There were over 1500 executives affected by the original bill's restrictions on new golden parachutes.[192] Of them, roughly fifteen are brought within the more restrictive framework of President Obama's restrictions for banks receiving "exceptional" funding.[193]

---

188 *See supra* Part III.B.1 for discussion concerning prospective applications.

189 For a discussion of how best to address those failures, *see infra* Part V.

190 *See supra* note 36 for discussion.

191 *See* Transactions Report, *supra* note 36.

192 The original EESA exempted banks in which the Treasury invested through "auction" purchases. *See* EESA § 111 (c). As a practical matter, nearly all of the Treasury's investments were made through direct purchases. *See* Transactions Report, *supra* note 36. In essence, the top five executives at nearly every institution funded by TARP were subject to EESA's executive compensation restrictions.

193 *See* TG-15, *supra* note 26. The executives from AIG, CitiGroup, Bank of America, and a few others are subject to additional limitations on the compensation of their top 100 earners through executive order. *See* Solomon, *supra* note 156. Congressional action subjects them to limitations on bonuses and severance, both of which are derivatively limited by the compensation limitation imposed by the aforementioned executive order. *Id.* All banks that accepted funding after February 11,

The TARP amendments in the stimulus bill increased complexity by creating new categories of covered employees.[194] For instance, the number of covered employees was reduced by four (to cover only the CEO) for banks in which the Treasury's position is less than $25 million.[195] For institutions holding more than $250 million of governmental investment, the restrictions cover at least triple the number of employees (fifteen) that were covered under TARP's original provisions.[196] Finally, institutions with $500 million or larger investment face restrictions on the compensation for at least five times as many employees (twenty-five) than were covered by the EESA previously.[197]

In all, more than 10,000 employees and executives could fall within at least one category of compensation restrictions.[198] A few of those will face the full brunt, with the attendant uncertainty, of the overlapping requirements of two potentially controlling statutes, a Treasury Regulation, an executive order, the contractual term sheet between the Treasury Department and the executive's institution, the review of a compensation-dedicated administration official, along with any individual waivers negotiated before

---

2009, face limitations on bonuses and severance for the top five executives. *See* ARRA § 7001 (amending EESA § 111 *et. seq.*).

[194] *See* ARRA § 7001 (amending EESA § 111(b)(3)(D)).

[195] *Id.* (amending EESA § 111(b)(3)(D)(ii)(I)).

[196] *Id.* (amending EESA § 111(b)(2)(D)(ii)(III)) (applying restrictions to the "senior executive officers and at least the 10 next most highly-compensated employees, or such higher number as the Secretary may determine is in the public interest").

[197] *Id.* (amending EESA § 111(b)(2)(D)(ii)(IV)) (applying restrictions to "the senior executive officers and at least the 20 next most highly-compensated employees, or such higher number as the Secretary may determine is in the public interest").

[198] *See id.* (amending EESA § 111(f)).

> [R]eview bonuses, retention awards, and other compensation paid to the senior executive officers and the next 20 most highly-compensated employees of each entity receiving TARP assistance *before* the date of enactment of the American Recovery and Reinvestment Act of 2009, to determine whether any such payments were inconsistent with the purposes of this section or the TARP or were otherwise contrary to the public interest.

Id. (emphasis added). If the Treasury Department were to blindly follow this mandate, it would be tasked with reviewing every payment made to the top twenty-five employees of every funded institution between October 2008 and February 2009. Given the 359 banks in which the Treasury held an interest in February of 2009, a number that has since nearly doubled, the Department had a mandate to thoroughly review nearly 9,000 personnel files—and even that number assumes that the composition of each bank's management team remained unchanged during the relevant period. *See* Tse, *supra* note 30.

the consummation of the original securities purchase.[199] The most regulated group will be the top five executives of banks that received funding from the first half of the TARP program, and were classified as an institution receiving exceptional aid after new guidelines issued on February 4, 2009. The least regulated group will be comprised of individuals hired after the stimulus bill was passed.[200] In between those extremes lie the rest of the regulatory scheme, and more than 10,000 employees.

As if sorting through the personnel files of some 10,000 employees to assess each individual's status under statutory, regulatory, and contractual provisions was not difficult enough, even determining which agency must enforce certain executive compensation restriction may prove a herculean task. For one, no single agency, including the pay czar, has the competency or jurisdiction to monitor all regulated executives: many of the regulated individuals work at publicly traded companies, and many others work for privately held entities.[201] Certain compensation restrictions can be waived by a simple vote of the shareholders, a process that will fall within the jurisdiction of both the SEC (as the regulatory authority that oversees shareholder action) and the Treasury Department in its role as the guardian of TARP funding.[202] There is little if any direction as to how the shareholder voting requirements will apply to privately held institutions, particularly those that do not utilize the corporate form.[203] The amended version of EESA § 111(b)(4) places the SEC in charge of certificates of compliance concerning executive compensation, to be filed by publicly-traded, funded institutions.[204] But there is no explicit delegation of oversight with respect to the amended requirements of § 111(c)—that each institution utilizes an independent executive compensation committee—a function that seems to be uniquely within the SEC's expertise.[205] Perhaps most importantly, there are few satisfactory guidelines as of yet that address how the SEC is to fulfill its role and in what way that its actions should complement the Treasury

---

[199] All of which fall under the purview of the Department of Treasury. ARRA § 7001 (amending EESA § 111(h)).

[200] This is a simple deduction of logical consequence. Any qualifying individual working prior to the stimulus bill would be subject to the retroactivity of its provisions.

[201] The amended § 111(e) entrusts the SEC with enforcing the toothless requirement that each publicly institution conduct non-binding shareholder voting for certain executive compensation decisions. *See* ARRA § 7001.

[202] In fact, Congress explicitly designated both agencies with responsibility for portions of TARP's enforcement. *See* ARRA § 7001 (amending EESA § 111 *et seq.*).

[203] For instance, the financial arms of both General Motors and Chrysler are organized as LLCs. *See* Transactions Report, *supra* note 36.

[204] *Id.*

[205] *See* ARRA § 7001 (amending EESA § 111 *et. seq.*).

Department, which has the broad responsibility to enforce TARP as a whole. The cooperation of the two agencies will be vital to the effective implementation of TARP's executive compensation restrictions.

Moreover, the original purpose of the TARP program—to inject liquidity into the nation's financial system to preserve the free flow of credit—is now lost in the cloud of administrative uncertainty.[206] Instead of concentrating upon the financial viability of funded institutions, precious Treasury resources must be allocated to address congressional concerns over the tangential issue of executive compensation.[207] Amid outcry from political leaders demanding a greater oversight and understanding of the disposition of TARP investment funds, Congress decided to further distract the Treasury Department from this task.[208] In light of this distraction, the Treasury is left to choose one of three paths: (1) expand its capacity and increase its spending in order to thoroughly address congressional concerns over both the broader oversight of TARP funding and the extremely narrow area of employee compensation, (2) maintain its planned course and divert resources originally allocated to TARP oversight to more closely scrutinize employee compensation, or (3) ignore the congressional mandate to oversee executive compensation altogether.[209] Given the broad authority granted to Kenneth Feinberg, it appears that option three was dead on arrival.

Additionally, defending TARP from litigious attack will absorb substantial resources. Executives who have been ousted will certainly look to sue their former employers if they are denied contractually guaranteed

---

[206] *See* EESA § 2(1).

[207] The Treasury could, for instance, allocate more resources to monitoring the financial viability of the funded institutions in what has become known as the Department's "stress test" for troubled banks. *See* David Ellis, *Treasury Unveils "Stress Test" for Banks*, CNN, Feb. 25, 2009, http://money.cnn.com/2009/02/25/news/companies/banks_test/index.htm.

[208] *See Angry Senator*, *supra* note 24. One of the most interesting political developments in the wake of the initial TARP distribution is the congressional response to perceived abuse by funded institutions. While much of the economic concern focused upon the availability of credit to individuals and businesses alike, nearly all of the rhetorical venom was directed at the executive officers of the funded institutions. Though the actions of these officers in approving discretionary bonuses were classified as "wasteful" or even "shameful," little effort was made to link the bonuses to the underlying "credit freeze." *See* Stolberg & Labaton, *supra* note 23. Thus, it can certainly be argued that the administration costs that will result from executive compensation restrictions will be incurred in the name of political expediency, and not in furtherance of the underlying economic policies TARP was intended to address.

[209] The proper balance among these outcomes is explored more thoroughly, *infra* Part V.A.

severance payments.[210] Given the size of the likely litigation,[211] the contractually-bound banks will need to weigh the options carefully.

The banks could pay out the contract amounts, and hope that either the Treasury does not notice or decides that the restrictive provisions would be unenforceable in court. The Treasury Department should certainly consider foregoing enforcement, because many of the provisions are at least colorably suspect under constitutional principles.[212] If the Treasury does decide that some action should be taken, it must be careful not to overplay its hand and unnecessarily drain capital from the institution through litigation or divestment of preferred shares. To go too far would frustrate the underlying liquidity-enhancing purposes of TARP.[213] Additionally, it is not entirely clear to what extent the Treasury could recover from the bank, especially in light of the heightened scrutiny paid to government officials when administering the government's contracts.[214] The Treasury could attempt to recover the payments directly from the ousted executive, but seizing funds from individuals for public use presents notable problems with respect to the Takings Clause.[215]

---

210 Remember John Thain? His ouster from Bank of America following the Merrill Lynch merger came with a door prize—all of the blame for a reported $15.3 billion in losses. *See* Creswell & Story, *supra* note 123. If Bank of America does fail to honor his contract, does anyone think that he would forego litigation? Granted, the term sheet between Bank of America and the Treasury required a waiver of claims by the Senior Executive Officers of the bank, but the effectiveness of that waiver may be called into question given the changed circumstances brought on by subsequent legislation. *See* Securities Purchase Agreement § 1.2(d)(v), *supra* note 15.

211 Thain, after all, took control of Merrill Lynch after the brokerage firm paid out $160 million to his predecessor pursuant to his exit clause. *See* Gogoi, *supra* note 124. The potential size of these battles may already be affecting the positions of all parties involved. After, Ken Lewis, Kenneth Feinberg, and Bank of America were able to amicably agree that Ken Lewis would forego and repay all of his 2009 salary, presumably in order to avoid a battle over his bulky retirement package. *See* Yousuf, *supra* note 124.

212 *See* discussion *supra* Part III. This, in fact, was Treasury's approach in the wake of hundreds of millions of government-subsidized bonuses at AIG. Despite the existence of a so-called pay czar, a large percentage of "retention bonuses" paid to AIG employees has remained in the hands of those employees. *See* David Goldman, *AIG Bonuses: $235 Million to Go*, CNNMONEY.COM, July 10, 2009, http://money.cnn.com/2009/07/10/news/companies/aig_bonuses/index.htm?postversion=2009071014. Most money that has been returned from these pay-outs has been returned voluntarily, after many employees succumbed to the immense political pressure and public outcry that followed these payments. *Id.*

213 *See* EESA § 2(1).

214 *See* Perry v. United States, 294 U.S. 330 (1935).

215 *See supra* Parts III.A.2, III.B.2.

If the banking institution decided to forego payment of its contractual obligations in order to avoid Treasury scrutiny, litigation would likely ensue between the bank and the ousted executive. Having no direct claim against the government, the executive would bring claims against the bank under contract, employment,[216] and constitutional theories.[217] Even if sovereign immunity prevents the government from being made a party to the action, the Treasury would likely spend immense resources compiling amicus briefs, and may choose to join such action voluntarily.

In all, the Treasury Department faces a heavy burden: it must administer policies that affect thousands of individuals and hundreds of banks; it must incorporate two statutes, multiple regulations, and enumerable individual contracts; and it will almost certainly face complex litigation. Under optimal conditions such an administrative burden would be less than ideal. The conditions, however, are far less than optimal. The Treasury is already tasked with the burden of overseeing the real body of TARP, and the Department is in no position to deal with the side show that is the program's executive compensation restrictions, pay czar or no pay czar.

B. *Economic Incentives—and Disincentives—Provided by Executive Compensation Limitations*

Despite reviewing constitutional, administrative, and other legal ramifications derived from the continued enforcement of executive compensation limits, no attention has yet been paid to whether the current system can or will have the effect that it was designed to have.[218] Will the current regulatory scheme result in an efficient return on the taxpayers'

---

216 State-based wrongful discharge claims might be a preferable course of action for both the executive and the defendant-bank. While the tax code has strict restrictions on the amount of deduction available to the bank for making a golden parachute payment, the company stands to recognize a larger portion of the money as a deduction if it can characterize the payment as an ordinary and necessary tort expense. *Compare* 26 U.S.C. § 280G (limiting the allowable deduction for golden parachute payments to an amount determined by a "base formula"), *with* Commissioner v. Tellier, 383 U.S. 687, 694–95 (1966) (holding that the expense of defense litigation is a deductible "ordinary and necessary" expense within the meaning of 26 U.S.C. § 162(a)).

217 Either way the constitutional issues would be resolved. The bank could not use a constitutionally void statute as an excuse to avoid paying its contractual obligations. Similarly, the close relationship—indeed ownership—between the bank and the Treasury Department would almost certainly be enough to sue the bank under constitutional theories as a concerted state actor.

218 Of course, if many of TARP's restrictions are eventually deemed unconstitutional, the current system will certainly fail to have the effect that Congress desires. *See supra* Part III.

investment in troubled banks, while ensuring that the banks themselves remain viable business enterprises? More specifically, do TARP's restrictions upon executive compensation actually further the underlying legitimate purposes of the program?

One could argue that the executive compensation provisions themselves bear little direct relationship to solving the broader financial crisis the statute was meant to address. The EESA itself defines the problem addressed by TARP as being one of liquidity.[219] Moreover, the sums of money doled out to address this liquidity problem rambles well into the billions.[220] Relatively small amounts of cash doled out to a select group of executives to whom the money is owed would have little effect.[221] Furthermore, much of the economic value of most severance packages is not accounted for in cash and would have little to no negative effect on liquidity,[222] but the EESA's provisions do not limit the statute's application to cash payments.[223] In fact, even if it were conceded that the total value of a golden parachute payments were the proper measure for the provision's effect on the institution's health, one can hardly say that even an exorbitantly large exit package would have any substantial impact in light of the size of Treasury holdings in distressed companies.[224]

Even if the amount of assets set aside for golden parachute provisions were indeed significant, it does not necessarily follow that freezing those assets would in any way free up cash for the redemption of the government's preferred shares. Though exit packages for many executives are structured as "unfunded" retirement plans in order to avoid ERISA's anti-discrimination provisions, certain assets may still be legally shielded from *equity* holders if

---

219 EESA § 2(1). As concluded, *supra* Part IV.A, much of the discussion concerning executive compensation misses the real issue addressed by TARP—the financial health of the nation's banking industry.

220 In just the initial implementation of TARP, Citigroup, JPMorgan Chase, and Wells Fargo each received $25 billion, with Bank of America receiving $15 billion. Snow, *supra* note 140.

221 *See Golden Parachutes of the Past Year: Robert L. Nardelli*, *supra* note 124. Even Bob Nardelli's legendary exit package included "only" $20 million in cash (less than ten percent of his overall package).

222 Some severance benefits, such as stock purchase options, could actually result in eventual cash inflows to a struggling firm. Though the future purchase of stock options may result in an overall dilution of shareholder value, the purchase itself would result in an increase in the bank's liquidity resulting from the cash infusion.

223 *See* ARRA § 7001 (amending EESA § 111(a)(2)).

224 A $200 million dollar golden parachute package would amount to 0.4% of the amount the Treasury had invested in Citigroup as of March 1, 2009. Transactions Report, *supra* note 36.

they are pledged for these plans.[225] These funds, potentially held in what are called "Rabbi Trusts" or other similar accounts, could not be shielded from general creditors without implicating ERISA.[226] They are not, however, part of the corporations' general funds and would be protected generally from the firm's equity holders, such as the Treasury Department.[227]

What is perhaps most disturbing is that the government's current position on various forms of executive compensation may actually inhibit the recovery process for many banks.[228] The executive compensation restrictions embodied in the American Recovery and Reinvestment Act of 2009 are no doubt restrictive enough to ensure that some institutions will, if they have not already, expedite the redemption of TARP shares.[229] But while Senator Dodd's goals of repayment will certainly be advanced by the restrictions, the incentives that he has provided pit the executives' interests against the interests of their institutions.[230] Executives at funded institutions will continue to want to divest the government as soon as possible in order to resume the benefits of their employment,[231] but questions remain as to whether such divesture would be good for a given company.[232] The misalignment of an executive's incentives with his company's goals will be especially noticeable for executives with sizable severance provisions.[233]

---

225 *See* Rev. Proc. 92-64, 1992-2 C.B. 422.

226 *Id.*

227 *Id.*

228 *See* Lucian Bebchuk, *Congress Gets Punitive on Executive Pay: We Want Compensation Tied to Performance*, WALL ST. J., Feb. 17, 2009, at A15. Professor Bebchuck has been an outspoken critic of outlandish executive compensation for years, but even he questions the efficacy of the TARP-related restrictions. *Id.*

229 *Id.* Most believe that the compensation restrictions were at least in part responsible for Goldman Sachs' decision to quickly redeem the Treasury's stake in the company. *See* OFFICE OF FIN. STABILITY, *supra* note 156.

230 *Id.*

231 As mentioned, the rush to get out from underneath the government's thumb is already underway, and ten banks moved to redeem Treasury-held shares as early as June 2009. *See Treasury Allowing 10 Banks to Repay TARP Money*, FOX NEWS, July 9, 2009, http://www.foxnews.com/politics/2009/06/09/report-allow-banks-repay-tarp-money/.

232 *See id.* In this respect, newly minted executive compensation restrictions seem to be in direct conflict with the original purposes of the TARP program. *See* EESA § 2(1). Despite initial congressional concerns about availability of credit, rationale lead executives will direct any cash surpluses to divesting the government instead of issuing new loans.

233 As discussed, the timing and structure of Ken Lewis's retirement from Bank of America undoubtedly was influenced by delicate negotiations with the Treasury over his salary and retirement package. *See* Yousuf, *supra* note 124. Given that the ARRA prohibits all severance payments, it will most certainly also affect the behavior of

Despite that TARP's executive compensation restrictions are meant to incentivize executives to redeem Treasury shares, the breadth of congressional policy now extends to limit the bonuses of many non-controlling employees.[234] Congress could have stopped short of regulating such personnel, but instead decided to limit the ways in which funded institutions could pay top performers.[235] Most surprisingly, Congress did not seek to limit the total compensation of individuals, and instead chose to limit the compensation mechanism through which the employer could reward its employees for performance.[236] Why Congress would make such a decision is nearly incomprehensible, and the policy will produce unintended consequences on a plethora of fronts.

First, the top performers at funded institutions now have every incentive to leave their current employer in favor of a less restrictive environment. Many regional banks that have eschewed funding are thus well positioned to absorb this talent, thereby shifting the competitive balance of the banking industry.[237] In fact, as some institutions divest the Treasury either by necessity or preference, they too will benefit from the talent that will almost certainly bleed from other banks. Of course, the result will be that institutions with the longest projected relationships with Treasury will have the greatest difficulty retaining top people. As those top people leave, it will be even more difficult for those institutions to post sufficient profits to quickly repay the Treasury.

Second, in order to stay competitive in the market for human capital, heavily leveraged institutions will look to alter pay structures to compensate for statutory restrictions. Many companies will shift toward higher salaries

---

executives that can expedite government divesture in preparation for planned career moves such as retirement. In fact, this is a key factor many experts believe to have hastened repayment from many of the already-divesting institutions. *See Treasury Allowing 10 Banks to Repay TARP Money*, *supra* note 231.

[234] *See* Bebchuk, *supra* note 228.

[235] *See* ARRA § 7001 (amending ESA § 111(b)(3)(D)).

[236] *See id.* (prohibiting the payment of any bonus in excess of one-third the employee's yearly salary).

[237] The FDIC insures 6995 commercial banks. *See* FDIC, STATISTICS ON DEPOSITORY INSTITUTIONS STANDARD REPORT 1, (2008), http://www2.fdic.gov/sdi/main.asp (Select "Retrieve Predefined Standard Reports" and the "Run Report" next to "Standard Report #1"). Only 359 banks had received federal funding and were subject to TARP's executive compensation restrictions as of February of 2009. *See* Tse, *supra* note 30. Even at TARP's peak, only 651 institutions had received funding. *See* Press Release, *supra* note 36.

and eliminate now undesirable performance based structures.[238] Under a less restrictive regulatory regime, companies would have been free to alter the terms of their bonus structure to maximize performance in the context of current financial realities.[239] But survival now mandates a shift in focus from maximizing the performance of top performers to simply retaining those same workers. Salaries will increase and so will the attendant fixed costs. Simultaneously, there will be little external incentive to encourage performance.

Far from advancing TARP's overall purposes, executive compensation restrictions act in many ways to torpedo the success of the governmental bail out of the banking industry. Troubled firms are left with fewer tools to motivate, attract, and retain high performing executives and employees alike, lengthening the road back to healthy profits. Controlling executives are tempted to consider their own pecuniary interests in divesting the Treasury Department of its shares regardless of whether such divesture is in the best interest of the company, the shareholders, or the nation.[240] Finally, it is unclear that *any* restrictions were needed in the first place, as executive compensation packages at worst presented a fractional drain upon the financial institutions' liquidity. Whatever history will say about TARP's success on the whole,[241] its executive compensation restrictions are unnecessarily burdensome and destructive of the program's purposes.

---

238 Performance based bonus plans are now undesirable on two fronts. First, they are limited in proportion to each covered employee's underlying salary. *See* Tse, *supra* note 30. Second, they can only be paid in the form of non-redeemable company stock. *Id.*

239 Indeed, funded institutions maintained much of this freedom even following President Obama and Secretary Geithner's restrictions imposed on the eve of the stimulus' passing. *See* TG-15, *supra* note 26.

240 Notice the other hidden failure of the current design: executives are now forced to consider *more* stakeholders than before in the fulfillment of their roles, while directors have *fewer* tools with which they can seek to align the executives' interest with the proper stakeholders. Ordinarily, compensation packages are designed, albeit with limited success, to align executives' personal incentives with the shareholder's goals. *See* Bebchuk, *supra* note 228. Now the packages create a three-way split, where the executives' personal incentives are misaligned with both shareholder interests and national interests. *Id.*

241 By many measures, TARP appears to be a success. In addition to on ongoing market recovery, several institutions have already redeemed the Treasury's equity positions. *See* OFFICE OF FIN. STABILITY, *supra* note 156. Moreover, TARP shares had generated over $9 billion in dividends for the Treasury by the end of August 2009. *Id.*

V. CONCLUSION: MOVING FORWARD WITH LITTLE GUIDANCE AND BIG GOALS

Wading through the morass of overlapping executive compensation restrictions placed upon TARP-aided firms is a daunting task. Both Congress and the Treasury Department have a responsibility to ensure that the policies are applied consistent with the Constitution. The Treasury Department has the additional burden of overseeing the administration of all TARP related regulations, cooperating with the SEC, and doing so in a way that strikes the proper balance between promoting healthy banks and protecting taxpayers' interests.[242] Corporations who have received these funds have the duty to protect the short and long-term interests of their shareholders, and the attendant social responsibility to treat their employees (including executives) fairly in light of the government regulation. Executives and other highly compensated employees have rights, existing both in contract and tangible property, which they can and should vigorously defend from government interference. The discussion below examines several methods through which each entity could properly and effectively portray its role as TARP moves forward.

A. *How Can the Treasury Department Responsibly Implement Current Policies?*

The Treasury Department, for its part, will be asked to oversee the regulatory regime by monitoring the actions of funded institutions and enforcing the legislative and executive policies imposed on those institutions.[243] In carrying forward that task, the Department and its accompanying pay czar will have to keep in mind competing policy goals: balancing financial liquidity in the banking sector,[244] on one hand, and the efficient redemption of shares currently held by the Treasury, on the other. Still these goals cannot be pursued through limitless means, and the Treasury Department must consider whether its actions are constitutionally defensible—to ensure both the legitimacy of its actions and to protect it from the costs of litigation.[245]

The Treasury has already taken some steps to address its litigation exposure. First of all, from the inception of the program the Treasury has

---

242 *See supra* Part IV.A.

243 *Id.*

244 *See* EESA § 2(1).

245 *See supra* Part III.

sought waivers of claims from firms to which it provided funding.[246] Though the waivers do not ensure shelter from all litigation costs with respect to executive compensation plans, they initially insulated the Treasury from suit.[247] In the wake of the retroactive overhaul of EESA § 111, the term sheet waivers are less airtight. At the time of contracting, none of the executives could have imagined the stringent wage, bonus, and severance restrictions that would follow.[248] In order to minimize potential litigation, the Treasury must seek to negotiate directly with the executives of banks who continue to hold federal money, as pay czar Kenneth Feinberg did with Ken Lewis.[249]

Additionally, the Treasury should look to enforce current statutory restrictions in a method that reasonably considers the aims of TARP. Though one of TARP's goals is certainly to ensure that taxpayers are repaid for the government's investments,[250] it makes no sense to enforce the protective provisions of the regulatory scheme in such a way as to jeopardize the financial viability of the member institutions.[251] This means that the Treasury cannot enforce policies in a way that promotes the redemption of Treasury shares when it would be financially risky for the bank to redeem those

---

[246] *See* 31 C.F.R. § 30 (2008).

[247] Remember that the term sheets connected to the purchase of preferred shares require the Senior Executive Officers (as defined by EESA § 111) to sign a waiver of claims against the Treasury Department as a condition of closing. *See, e.g.*, Securities Purchase Agreement § 1.2(d)(v), *surpa* note 15. The term sheets also require that the company align all benefit plans with EESA § 111. *See id.* § 4.10. The term sheets themselves do not require any employee or executive to waive claims against the *employing institution* for breach of contract, although the individual waivers of the executives may be very broad. The Treasury Department could become an indirect party to an action against the employing institution on claims that are not covered by those individual waivers. *See supra* Part IV.A.

[248] Newer statutory restrictions clearly apply in many previously unforeseen circumstances: all severance packages exceeding one year's compensation, all "bonus and incentive" payments exceeding one-third of annual salary, executives at all banks regardless of the amount of federal investment, highly compensated employees (besides executives) at banks receiving more than $500 million. No reasonable court could construe the original waivers of claims to encompass these unforeseeable retroactive changes in the law.

[249] *See* Yousuf, *supra* note 124.

[250] *See* EESA § 2(1).

[251] *See supra* Part IV for a discussion of the primary purpose of TARP—stabilizing the nation's banking system. It should be pointed out that the best method of protecting the taxpayer's "investment" would have been to avoid investing in the first place. Because Congress clearly rejected this approach, it can be assumed that they would support a position that favored quick repayment *over* a healthy banking institution.

shares.[252] It likewise means that the Treasury should be careful not to force a bank to cede its top talent to competitors, in order to fulfill its short-term obligations.[253]

Finally, the Treasury Department should decline the congressional invitation to clawback executive bonuses that were paid out following the first round of TARP investments.[254] Such an unprecedented action would almost certainly be struck down by a court as an unconstitutional taking of property.[255] As long as the statute is in place, the Treasury may use the threat of clawback as the proverbial stick when negotiating the intricacies of other TARP related transactions. Perhaps that is all that is intended by pay czar Kenneth Feinberg's public declaration of his intent to pursue such clawbacks.[256] What the Department should not do is cross the constitutional line, blindly following Congress' misguided lead.

These suggestions can be summarized quite easily: the Treasury Department needs to logically prioritize its objectives. The present crisis provides no occasion to forego constitutional principles. Prevention is often cheaper than remuneration, and it will likewise be cheaper to seek executives' consent than to force their submission.[257] Most obviously, big numbers outweigh the small, and it would be foolish to risk the stability of a multi-trillion dollar industry to unduly limit the compensation of million dollar executives.

B. *What Should Congress Do to Alleviate Self-Created Problems?*

Although the Treasury Department can ameliorate the consequences of congressional action through the aforementioned waivers and reasonable

---

[252] A bank at risk, for instance, of either losing its top talent or lawsuit from a highly compensated employee, might be motivated to redeem preferred shares prior to the stabilization of underlying market problems.

[253] After all, this is quite the Hobbesian choice. In order to avoid insolvency in the near term, a bank might be forced to unreasonably limit the compensation of key employees. However, if those same employees left by either necessity or choice, the same bank may not remain competitive in the long and medium terms, creating a future risk of insolvency.

[254] *See* ARRA § 7001 (amending EESA § 111(f)). Up until now, the Treasury appears to be following this advice. *See* Goldman, *supra* note 212. Of course, as long as the statute maintains its current language, Treasury's position could shift to meet the prevailing political wind.

[255] *See supra* Part III.B.2.

[256] *See* Wutkowski, *supra* note 157.

[257] Indeed, consent is the mechanism through which most of the AIG bonus-reductions have occurred. *See* Goldman, *supra* note 212. It is also the mechanism through which Ken Lewis's 2009 salary and bonuses were recouped. *See* Yousuf, *supra* note 124.

construction, Congress should not sit idly. The literal language of existing statutory law could result in unreasonably low compensation for executives who, in good faith, volunteered for salary reductions in the wake of financial crisis.[258] Additionally, the restrictions are now so oppressive as to create tension between the twin purposes of TARP.[259] Finally, certain of TARP's retroactive provisions are so blatantly in violation of constitutional principles that Congress should act quickly to repeal those restrictions.[260]

As an initial matter, Congress should enact at least a limited exception to its prospective limitations on executive bonuses. Executives such as Vikram Pandit, the CEO of Citigroup, who have voluntarily lowered their salaries during the financial crisis, should not be punished by the EESA's harshest restrictions.[261] If Congress is dedicated to the preservation of the underlying limitation,[262] the policy can be preserved by allowing executives who take voluntary salary reductions to inflate the allowable percentage of *performance* bonus payment to offset the loss. In addition to relieving the unfair burden on good Samaritan CEOs, this change would have the side effect of allowing financial institutions to retain some of their talent while shifting money from executive salaries into performance based incentives.

While considering a safe harbor for executives that voluntarily accept lower salaries, Congress should also consider softening its extreme positions on a few other issues as well. While it may indeed be good policy to restrict true golden parachute payments,[263] the current definition sweeps so broadly as to cause even solid performing executives to protect their own retirement—whether or not it is in the best interest of the company and the nation.[264] Though a narrower definition of golden parachute comes with its

---

[258] For instance, Vikram Pandit of Citibank offered to accept a one dollar per year salary during the crisis. *See* Elizabeth Hester, *Citigroup's Vikram Pandit to Take $1 Salary, No Bonus*, BLOOMBERG.COM, Feb. 11, 2009, http://www.bloomberg.com/apps/news?pid=20601103&sid=a86BGz.hIWd0&refer=us. Though Pandit's pledge included a disclaimer of bonus rights in the short term as well, current statutory law limits his bonuses to roughly thirty-three cents per year, payable in non-redeemable company stock. *See* ARRA § 7001 (amending EESA § 111(b)(3)(D)(i)). Though it is possible that Congress intended this result, it seems more likely that Congress failed to think about it at all.

[259] *See supra* Part IV.A.

[260] *See supra* Part III.B.2.

[261] *See* Hester, *supra* note 258.

[262] A dedication which may be misplaced. *See supra* Part IV.B.

[263] Such as the payments made when an executive is forced out for bad performance through bankruptcy or change of control. *See* discussion *supra* note 121.

[264] Veterans like Mack Whittle have already left the business to protect such interests. *See* Kiel, *supra* note 21.

own difficulties—such as unwinding interrelated guarantees for retirement and change of control—a narrower definition also would allow executives' to retire at the natural end of their careers without having to decide between personal security and corporate stability.[265]

Most importantly, Congress should act quickly to remedy an egregious constitutional error. The newly amended EESA § 111(f) empowers the Treasury Department to clawback bonus payments made to covered executives prior to the Act's passage.[266] Although exorbitant executive bonuses make for compelling political theater,[267] once those bonuses have been paid the Fifth Amendment prohibits the government from seizing that money for itself.[268] Even if the Treasury Department were to follow the sound advice of this Note and ignore the mandate of EESA § 111(f), Congress should still act to correct its error. TARP's size and scope are suggestive of a program that will last for years, and future administrations should not be left with a statutory mandate to affect an unconstitutional taking of private property.

C. *In What Ways Can Individuals and Companies Protect Their Interests?*

Even as Congress and the Treasury Department sort through their respective responses to an unworkable regulatory scheme, institutions that received TARP funding—as well as executives and highly compensated employees—should begin the process of self protection.

1. *Protecting Institutional Interests*

As funded institutions stare down a regulatory scheme that severely limits flexibility with respect to executive compensation,[269] the companies must still consider the individuals to whom they owe duties. Corporations' obligations to their shareholders through ownership and employees through contract have not disappeared, and funded institutions must be mindful of these two stakeholders when navigating through TARP's restrictions on executive compensation.

---

265 Recall that current incentives may prompt executives to redeem Treasury-held equity while it is not financially prudent to do so. *See supra* Part IV.B.

266 ARRA § 7001.

267 *See* Stolberg & Labaton, *supra* note 4.

268 *See supra* Part III.B.2.

269 *See supra* Part IV.B.

Corporate shareholders are still entitled to the protections provided to them by a board's fiduciary duties. Whether for better or for worse, the misaligned incentives created by congressional heavy-handedness now constrain the flexibility of each firm's directors to promote shareholder prosperity. Instead of constructing contracts that contain heavy performance bonus incentives,[270] careful compensation committees must manufacture incentives by making large portions of an executive's *salary* contingent upon performance indicators. While some might find this a shareholder friendly outcome, the truth is that directors now have fewer tools to construct an appropriate compensation policy that fits the unique needs of an individual firm.

Directors must also guard against the temptation that executives might have to pursue strategies that will protect their retirement interest.[271] Banks must resist the urge to redeem Treasury shares in the name of convenience, and instead analyze the course of action that will be the most beneficial to shareholders in the long-term. While negotiating this internal minefield, better capitalized institutions—such as those approaching profitability—might benefit from reasonable lobbying investments aimed at re-aligning statutory incentives to maximize both personal and shareholder wealth.

Corporations must also be mindful of contractual obligations to top employees. When legal conflict is imminent, such as in the case of a likely employee suit for a breach of contract, the corporation will have to weigh the costs of defending the suit against the likelihood that the government can and will enforce TARP's executive compensation restrictions.[272] Funded institutions must rely upon their legal representatives for advice concerning the viability of both employee and governmental claims. Striking this balance will prove difficult, as the unique nature of the questioned restrictions provides a sketchy picture of likely judicial outcomes.[273]

2. *Protecting Individual Interests*

As stories circulate about heavy handed tactics used by the government to motivate large banks to utilize TARP funding,[274] individual executives

---

[270] A now-prohibited practice under the amended EESA § 111(b)(3)(D)(i). ARRA § 7001.

[271] A problem now that golden parachute payments are completely prohibited and include "any payment to a senior executive officer for departure from a company for any reason." ARRA § 7001 (amending EESA § 111(a)(2)).

[272] *See supra* Part IV.A.

[273] *See supra* Part III.

[274] *See* Dan Fitzpatrick, Susanne Craig & Deborah Solomon, *USA Inc.: In Merrill Deal, U.S. Played Hardball*, WALL ST. J., Feb. 5, 2009, at A1. Rumors surrounding Bank

and highly compensated employees must remain vigilant in their protection of personal rights. Some of TARP's restrictions likely fall squarely within the police power of Congress, and those provisions should remain unchallenged.[275] However, as certain provisions abrogate contractual rights and may delay precious benefits such as retirement, those provisions are ripe for litigation. Although not yet in direct use by the Treasury Department, the retroactive provisions contained in the amended EESA present another issue over which many executives should prime themselves for legal battles.

Executives who are contemplating retirement should discuss their intentions with the corporation's directors to determine whether the company plans to heed Congress' mandate and withhold payment. If the company does not intend to pay the obligation, an executive can protect her own interest by filing a claim against the employing company under the Declaratory Judgment Act or some state corollary.[276] Such a suit would benefit the executive by allowing for continued employment while the constitutional questions surrounding retirement were resolved in court.[277]

When and if the Treasury Department does begin enforcing EESA § 111(f) and its clawback provisions, executives should refuse to comply.[278] That the government could confiscate money from individuals who received such payment in compensation for work performed violates the most

---

of America's purchase of Merrill Lynch suggest that federal officials threatened to hasten the ouster of Bank of America's Board of Directors and CEO Ken Lewis if the company backed out of its bid for the troubled mortgage giant. *Id.* The resulting deal could not have been completed without the Treasury Department purchasing a bigger stake in Bank of America—to the tune of about $20 billion. *Id.* In effect, federal pressure to close the Merrill Lynch deal forced Bank of America to accept more federal financing, and the additional debt lengthened the period during which Bank of America's executives will fall under TARP's restrictions on compensation. *Id.*

[275] It is unlikely, for instance, that the prospective application of most of TARP's restrictions on bonus payments violates any constitutional provision. *See supra* Part III.B.1.

[276] *See, e.g.*, 28 U.S.C. § 2201 (2006).

[277] An executive would have difficulty pursuing a similar path with respect to unmatured claims under the retroactive provisions of EESA § 111(f). Until the Treasury Department begins attempting to recover bonus payments made prior to the passage of the stimulus bill, it would be difficult to establish that a controversy existed that would justify a court hearing the case.

[278] At least to this observer, it appears that Ken Lewis did exactly this. Though Lewis relinquished his 2009 compensation at the behest of Kenneth Feinberg, it seems that he may have avoided a fight over his much larger retirement package. *See* Yousuf, *supra* note 124. In effect, Lewis allowed Feinberg a political victory by acquiescing to a clawback in exchange for Feinberg's choice not to pursue Lewis's retirement benefits as a golden parachute.

hallowed of constitutionally guaranteed property rights.[279] That the Fifth Amendment protects each executive from the reach of the Treasury Department's seizure is, of course, a great personal benefit to the individual who wishes to keep her money. But the enforcement of that Fifth Amendment right will benefit the rights of many, as "eternal vigilance by the people is the price of liberty, and that you must pay the price if you wish to secure the blessing. It behooves you, therefore, to be watchful in your States as well as in the Federal Government."[280]

D. *Moving Forward*

The Employee Economic Stabilization Act of 2008 and subsequent statutory and regulatory modifications to its terms provide a rough outline for a complex economic strategy to ensure the short term stability and long term prosperity of the American financial system. Portions of the Act seek to set penalties, or at least withhold rewards, from the senior executives of the various banks and other institutions that have absorbed hundreds of billions of dollars of taxpayer money. While superficially noble and politically expedient, some of these provisions flirt with the outer bounds of sound reason and governmental power.

Wise policy supports many of the various prohibitions—such as barring new contracts with senior executives that provide exorbitant bonus structures. Other restrictions are self-defeating and undermine the very purpose for which the TARP program was designed.

Notwithstanding policy considerations, EESA provisions that apply retroactively to contracts—freely negotiated and legally sound—face some unique and nuanced constitutional challenges. Some of the constitutional hurdles can and will be avoided through judicial construction and reasonable agency application. Some of TARP's restrictions on executive compensation are so perverse that only an outright congressional repeal could cure the defect.

What is undoubted is that there is a heavy burden on the Treasury Department to administer a complex scheme of compensation restrictions, though the value of those restrictions is debatably insufficient to justify attention. In performing its duties, the Department must steer clear of policies that ignore fundamental rights, undermine the broad and important purposes of TARP, and unnecessarily detract focus from the oversight of large pools of money in favor of the scrutiny of small amounts. Most importantly, the crisis of the moment must not be the catalyst for the abandonment of long-treasured constitutional principles.

---

279 *See supra* Part III.B.2.

280 Andrew Jackson, President of the U.S., Farewell Address (Mar. 4, 1837).